S. Hrg. 99-1019

HOME AUDIO RECORDING ACT

HEARINGS

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

AND ITS

SUBCOMMITTEE ON
PATENTS, COPYRIGHTS AND TRADEMARKS

NINETY-NINTH CONGRESS

FIRST AND SECOND SESSIONS

ON

S. 1739

A BILL TO AMEND TITLE 17 OF THE UNITED STATES CODE WITH RESPECT TO HOME AUDIO RECORDING AND AUDIO RECORDING DEVICES AND MEDIA, AND FOR OTHER PURPOSES

OCTOBER 30, 1985; MARCH 25 AND AUGUST 4, 1986

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HOME AUDIO RECORDING ACT

WEDNESDAY, OCTOBER 30, 1985

U.S. Senate,
Committee on the Judiciary,
Subcommittee on Patents, Copyrights and Trademarks,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:30 a.m., in room SD-562, Dirksen Senate Office Building, Hon. Charles McC. Mathias, Jr. (chairman of the subcommittee), presiding.

Also present: Senators Metzenbaum, DeConcini, and Leahy.

Staff present: Steve Metalitz, chief counsel and staff director; Matthew Gerson, counsel; John Podesta, minority chief counsel; Pamela Batstone, chief clerk; Beverly McKittrick, counsel to Senator Laxalt; Ed Baxter, counsel to Senator DeConcini; and Eddie Correia, counsel to Senator Metzenbaum.

OPENING STATEMENT OF HON. CHARLES McC. MATHIAS, JR., A U.S. SENATOR FROM THE STATE OF MARYLAND

Senator Mathias. The committee will come to order.

The Subcommittee on Patents, Copyrights and Trademarks convenes today to consider the growing practice of unauthorized home audio taping of copyrighted material. The bill before us, Senate bill 1739, takes a balanced approach to the audio home taping problem. The bill would legalize the home taping of copyrighted music and other audio material in exchange for a modest royalty on the tools used to make those copies. The one-time royalty on the manufacturers and importers of the recording equipment and blank tapes would be distributed through the Copyright Royalty Tribunal to those who own the copyrights in appropriated materials. I want to emphasize that the bill will not affect the current status of video home taping and is not a precursor of similar legislation on videotaping.

As I look around the room today, I am reminded that many of us have been here before. However, we return to this issue because of the overwhelming evidence that advancing technology is impairing the ability of the copyright law to effectively promote innovation and artistic progress.

The underlying premise of the constitutional authorization for copyright legislation is to provide artists and authors an incentive to develop their talents so that the whole public can benefit from and enjoy their creations. Faithful to that premise, Congress has often been called upon to craft the changes necessary to maintain that incentive in the context of new technology. Just as this body had to react to the copyright issues raised by juke boxes and cable television in the 1976 Copyright Act, and by advances in computer software a few years later, so must we respond today to dual-port cassette decks, compact discs, and other technological advances that threaten to undermine the bargain contemplated by the Constitution. Senate bill 1739 is such a response, one that, in my view, improves on earlier initiatives in this field.

When unauthorized home taping diverts massive sums—perhaps $1½ billion each year—from sales of prerecorded music, the recording industry is not the only loser. Certainly performers, composers, producers, unions, backup musicians and backup vocalists all lose. But in addition, there is less money available for investment to cultivate new recording talent. That means that albums unlikely to soar to the top of the charts are not released. It means less support for less popular forms of music such as classical music and the uniquely American genres of jazz, folk, and gospel. It means, in effect, that all America and, indeed, the whole world loses something. At risk are not simply the blockbuster hits, but the diversity, the richness, and the vitality that have made American music a source of admiration around the globe.

So this issue involves not just rock and roll or Nashville and its superstars, but also the music that springs forth from America's conservatories and churches. The problem is not just teenagers and college students taping top-40 music but also adults who rely on widely circulated schedules to tape symphonic performances from the public airwaves. The Home Audio Recording Act rests on the recognition that the short-term gain to the consumers from unrestricted home taping is outweighed by the cost the whole society will ultimately have to pay in terms of damage to the rich American musical tradition. Our hearing this morning will explore the facts underlying that recognition, and the proposal for corrective action contained in Senate bill 1739.

[A copy of S. 1739 follows:]

99TH CONGRESS
1ST SESSION

S. 1739

To amend title 17 of the United States Code with respect to home audio recording and audio recording devices and media, and for other purposes.

IN THE SENATE OF THE UNITED STATES

OCTOBER 7 (legislative day, SEPTEMBER 30), 1985

Mr. MATHIAS (for himself, Mr. HATCH, Mr. D'AMATO, Mr. WILSON, Mr. COCHRAN, Mr. KENNEDY, Mr. CRANSTON, Mr. SASSER, Mr. GORE, Mr. SIMON, and Mr. LEAHY) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

---

A BILL

To amend title 17 of the United States Code with respect to home audio recording and audio recording devices and media, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Home Audio Recording Act."

SEC. 2. (a) Chapter 1 of title 17 of the United States Code is amended by inserting at the end thereof the following new section:

"§ 119. Limitation on liability: Audio recording

"(a) AUDIO RECORDING.—Notwithstanding the provisions of section 106(1), an individual who makes an audio recording of a musical work or a sound recording is exempt from any liability for infringement of copyright if the recording made is for the private use of that individual or members of his or her immediate household: *Provided, however,* That nothing in this section shall exempt from liability a person who, for purposes of direct or indirect commercial advantage, induces, causes or materially contributes to the making of audio recordings by any individual or entity.

"(b) COMPULSORY LICENSE FOR AUDIO RECORDING DEVICES AND MEDIA.—

"(1) AVAILABILITY OF COMPULSORY LICENSE.—Notwithstanding the provisions of section 106(1), the importation into and distribution in the United States, and the manufacture and distribution in the United States, of any audio recording device or audio recording medium shall be subject to compulsory licensing if the importer or manufacturer of the device or medium records the notice, and deposits the statement of account and total royalty fees, specified by this paragraph.

"(A) The importer or manufacturer shall, at least one month before the distribution in the United States of any audio recording device or any audio recording medium or within sixty days after the date this section becomes effective, whichever date is later, record a notice with the Register of Copyrights (hereafter in this section referred to as the 'Register'). Such notice shall include a statement of its identity and address and a description of any trade or business names, trademarks, or like indicia that it uses in connection with the importation, manufacture, or distribution of audio recording devices or audio recording media in the United States. Thereafter, from time to time, the importer or manufacturer shall record such further information as the Register shall prescribe by regulation to carry out the purposes of this paragraph.

"(B) The importer or manufacturer shall deposit with the Register, at such times, for such periods, and in accordance with such requirements as the Register shall prescribe by regulation, a statement of account, covering the pertinent period next preceding, specifying the number of audio recording devices or amount of audio recording media imported into or manufactured in the United States during such period, and the number or amount distributed in the United States during such period, together with such other information, and in such form, content and manner, as the Register shall from time to time prescribe by regulation. Such statement shall be accompanied by the total royalty fee specified in subsection (c) of this section for the period covered by the statement, computed in accordance with such regulations as the Register shall from time to time prescribe.

"(2)(A) INFRINGEMENT.—Notwithstanding the provisions of paragraph (1), the importation into and distribution in the United States, or the manufacture and distribution in the United States, of any audio recording device or audio recording medium is actionable as an act of infringement under section 501, and is fully subject to the remedies provided by sections 502 through 506, 509, and 511, if the notice, statement of account, or total royalty fee specified by paragraph (1) has not been recorded or deposited, or if the statement of account or total royalty fee does not materially comply with the requirements of paragraph (1) or any regulations prescribed thereunder.

"(B) Multiple audio recording devices shall not be subject to compulsory licensing under paragraph (1), and the importation into and distribution in the United

States, or the manufacture and distribution in the United States of such devices shall be actionable as an act of infringement under section 501, and shall be fully subject to the remedies provided by section 502 through section 506, and section 509.

"(3) DEPOSIT OF ROYALTY FEES.—The Register shall receive all fees deposited under this section and, after deducting reasonable administrative costs, shall deposit the balance in the Treasury of the United States, in such manner as the Secretary of the Treasury shall direct. All funds held by such Secretary shall be invested in interest-bearing United States securities for later distribution with interest by the Copyright Royalty Tribunal (hereafter in this section referred to as the 'Tribunal') as provided by this title. The Register shall promptly submit to the Tribunal a compilation of all statements of account covering the pertinent periods provided by paragraph (1).

"(4) COPYRIGHT OWNERS ENTITLED TO ROYALTY FEES.—The royalty fees deposited pursuant to this section in connection with audio recording devices and media shall, in accordance with the procedures specified in paragraph (5), be distributed to the owners of copyrights in musical works and sound recordings that were included in radio or television transmissions, or distributed to the public in the form of phonorecords or copies, during the period to which such fees pertain.

"(5) Distribution of royalty fees.—The royalty fees deposited pursuant to this section shall be distributed in accordance with the following procedures:

"(A) During the 30-day period specified by the Tribunal for each year after the year in which this section becomes effective, every person claiming to be entitled to compulsory license fees under paragraph (4) of this subsection shall file a claim with the Tribunal for fees covered by all statements of account for periods during the preceding year in accordance with requirements that the Tribunal shall prescribe by regulation. All such claimants shall negotiate in good faith among themselves in an effort to agree to a voluntary proposal for the distribution of royalty fees. Notwithstanding any provision of the antitrust laws, for purposes of this clause any claimants may agree to the proportionate division of compulsory licensing fees amongst them, may lump their claims together and file them jointly or as a single claim, or may designate a common agent to receive payment on their behalf.

"(B) After the first day of the month following the period established for the filing of claims under subparagraph (A), in each year after the year in which this section becomes effective, the Tribunal shall determine whether there exists a controversy concerning the distribution of royalty fees. If the Tribunal determines that no such controversy exists, it shall, after deducting its reasonable administrative costs under this subsection, distribute such fees to the copyright owners entitled to such distribution, or to their designated agents. If the Tribunal finds the existence of a controversy, it shall, pursuant to chapter 8 of this title, conduct a proceeding to determine the distribution of royalty fees. In making its determination, the Tribunal shall so far as possible give effect to any voluntary proposal for the distribution of royalty fees negotiated in accordance with subparagraph (A).

"(C) During the pendency of any proceeding under this subsection, the Tribunal shall withhold from distribution an amount sufficient to satisfy all claims with respect to which a controversy exists, but shall have discretion to proceed to distribute any amounts that are not in controversy.

"(c) ROYALTY FEES.—

"(1)(A) AUDIO RECORDING DEVICES.—The royalty fee payable under subsection (b) for each audio recording device imported into and distributed in the United States, or manufactured and distributed in the United States, shall be five per centum of the price charged for the first domestic sale of such device.

"(B) DUAL AUDIO RECORDING DEVICES.—The royalty fee payable under subsection (b) for each dual audio recording device imported into and distributed in the United States, or manufactured and distributed in the United States, shall be twenty-five per centum of the price charged for the first domestic sale of such device.

"(C) AUDIO RECORDING MEDIA.—The royalty fee payable under subsection (b) for each audio recording medium imported into and distributed in the United States, or manufactured and distributed in the United States, shall be one cent per minute of the maximum playing time or fraction thereof for such medium.

"(D) EXEMPTIONS.—The Tribunal shall by regulation exempt from royalty fees particular kinds of audio recording devices or audio recording media, if any, that the Tribunal finds, on the basis of technical criteria that are relevant to the purposes of this section, are unsuitable for making audio recordings by individuals for private use.

"(E) NONINFRINGING USES.—The Tribunal shall by regulation establish a procedure under which audio recording devices or audio recording media purchased and used only under the circumstances specified in this paragraph shall not be subject to payment of any of the royalty fees otherwise payable under subsection (b). Pursuant to this paragraph the Tribunal shall exempt from royalty fees audio recording devices or audio recording media that—

"(i) are purchased under circumstances where any part of the purchase price is deductible by the purchaser either as an ordinary and necessary business expense under section 162 of the Internal Revenue Code of 1954 or as an allowance for depreciation under section 167 of such Code, or, in the case of purchases by a nonprofit organization, would be so deductible if either section was applicable; and

"(ii) will not be used for making audio recordings by individuals for private use or for other infringing purposes in violation of this title.

"(2)(A) ADJUSTMENT OF ROYALTY FEES.—The fees specified in paragraph (1) shall be subject to adjustment by the Tribunal in the fifth calendar year after the date this section becomes effective, and in each subsequent fifth calendar year, in accordance with the petition procedure described in section 804(a)(2) of this title and regulations that the Tribunal shall prescribe. Notwithstanding the provisions of section 809 of this title, any final determination by the Tribunal in the first and any subsequent adjustment proceeding under this paragraph shall become effective thirty days following its publication in the Federal Register.

"(B) In determining royalty fees under this paragraph, the Tribunal shall consider, in addition to all other relevant factors, the following criteria:

"(i) the value to an individual of the right to reproduce copyrighted works pursuant to subsection (a) of this section;

"(ii) the compensation that would have been received by copyright owners from distribution in the United States of phonorecords of their sound recordings and musical works but for private audio recording of such works;

"(iii) the projected impact of royalty fees on consumers and the benefits derived by consumers from the use and availability of audio recording devices or media;

"(iv) the benefits derived by importers and manufacturers of audio recording devices or media from the distribution in the United States of those products;

"(v) the projected impact of private audio recording on copyright owners;

"(vi) the projected effect of royalty fees on the structure and financial condition of the audio recording device or media importing and manufacturing industries;

"(vii) the relative roles of copyright owners and importers and manufacturers of audio recording devices or media with respect to creative and technological contribution to the development of sound recordings and musical works;

"(viii) the objective of maximizing the creation of new sound recordings and musical works;

"(ix) reasonable estimates of the amount of audio recording devices or media used in the United States during a relevant period for purposes other than making audio recordings by individuals for private use if such purposes are lawful under this title; and

"(x) new technologies for making audio recordings by individuals for private use.

"(C) Any determination by the Tribunal under this paragraph may distinguish among different kinds of audio recording devices or audio recording media, and may establish different royalty fees for different kinds of audio recording devices or audio recording media.

"(d) DEFINITIONS.—As used in this section, the following terms and their variant forms mean the following:

"(1) An 'audio recording' is a phonorecord or aurally perceptible copy (without accompanying visual images) of a musical work or sound recording that has been reproduced directly from a radio or television transmission or from a phonorecord or copy that has been lawfully made and distributed to the public.

"(2) An 'audio recording device' is any machine or device, now known or later developed, which can be used for making audio recordings by individuals for private use, and which is capable of reproducing the sounds embodied in a radio or television transmission, or in a phonorecord or copy, by means of internal or external wire, cable or like connection between the equipment receiving or performing such sounds and the equipment reproducing them. The term 'audio recording devices' includes dual audio recording devices. Such term does not include a device (A) which is unable to receive the sounds embodied in a radio or television transmission, or in a phonorecord or copy, except by microphone; (B) which is capable only of performing such sounds (playback only equipment); or (C) which incorporates a decoder or similar mechanism that prevents the device from reproducing, or permits the device to reproduce, the sounds embodied in a phonorecord or copy in accordance with special instructions encoded in the phonorecord or copy for that purpose.

"(3) An 'audio recording medium' is any material object, now known or later developed, in any form commonly distributed for use by individuals (such as analog or digital tape cassettes, cartridges or reels), in which a musical work or sound recording can be fixed by use of an audio recording device. Such term does not include a material object that embodies a sound recording at the time it is first distributed by the importer or manufacturer, unless the sound recording has been so embodied in order to avoid the obligations of subsection (b).

"(4) A 'dual audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one cavity for the insertion of a phonorecord in any such format and one cavity for the insertion of an audio recording medium in any such format.

"(5) The 'first domestic sale' of an audio recording device is the first sale of such device in the United States to an unrelated party. For purposes of this paragraph, an unrelated party is a person who is not controlling, controlled by, or under common control with the seller, and who is not acting in concert with the seller in order to avoid or lessen the obligations of subsection (b). Control will be deemed to exist if there is a fifty per centum or greater direct or indirect ownership interest between the seller and such other person.

"(6) A 'multiple audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one or more cavities for the insertion of a phonorecord in any such format and two or more cavities for the insertion of an audio recording medium in any such format.

"(7) A 'radio transmission' and a 'television transmission' are transmissions by a broadcast station, cable system, multipoint distribution service, subscription service, direct broadcast satellite, or other means of transmission that are intended for reception in private homes.".

(b) The table of sections for chapter 1 of title 17, United States Code, is amended by adding at the end thereof the following new item:

"119. Limitation on liability: Audio recording.".

SEC. 3. (a) Chapter 5 of title 17 of the United States Code is amended by inserting at the end thereof the following new section:

"§ 511. Additional remedy for infringing importation or manufacture, and distribution of audio recording devices and media

"In any action filed pursuant to section 119(b)(2), the court may order that, in addition to any other remedies provided by this title, for a period not to exceed ninety days, the importer or manufacturer shall be deprived of the benefit of a compulsory license under section 119(b)(1). In the absence of such license by reason of such order, any importation into and distribution in the United States, or any manufacture and distribution in the United States, of audio recording devices or media by such party is actionable as an act of infringement under section 501, and is fully subject to the remedies provided by sections 502 through 506, 509, and this section.".

(b) The table of sections for chapter 5 of title 17, United States Code, is amended by adding at the end thereof the following new item:

"511. Additional remedy for infringing importation or manufacture, and distribution of audio recording devices and media.".

SEC. 4. Chapter 8 of title 17 of the United States Code is amended as follows:

(a) Section 801(b)(1) is amended by striking out "and 116," in the first sentence, and inserting in lieu thereof ", 116 and 119,".

(b) Section 801(b)(3) is amended by striking out "and 116," and inserting in lieu thereof ", 116 and 119,".

(c) Section 804(d) is amended by striking out "or 116," and inserting in lieu thereof ", 116 or 119,".

(d) The second sentence of section 809 is amended by striking out "or 116," and inserting in lieu thereof ", 116 or 119,".

SEC. 5. SUPPLEMENTARY AND TRANSITIONAL PROVISIONS.—(a) This Act, and the amendments made by this Act, shall become effective on July 1, 1987.

(b) Section 501(a) of title 17 is amended by striking out "118" and inserting in lieu thereof "119".

Senator Mathias. Before we call our first witness, let me ask the distinguished Senator from Ohio, Mr. Metzenbaum, to make a statement.

OPENING STATEMENT OF HON. HOWARD M. METZENBAUM, A U.S. SENATOR FROM THE STATE OF OHIO

Senator Metzenbaum. Mr. Chairman, I am always pleased when this legislation hits the congressional tables and comes before us. It gives us a chance to get off SDI and budget balancing and the farm bill. We do not even have an abortion proposal in this legislative proposal.

Senator Mathias. We may. [Laughter.]

Do not make any premature judgments.

Senator Metzenbaum. Often we get some prominent entertainment celebrities to come down and tell us how critical this legislation proposed is. We not only bring out all of the heavy-hitting lobbyists around Washington—they are all here. That is not particularly odd, because they are here regularly, but we also get a chance to see some people lobbying. We probably get more cards on the subject of this kind than any other, more newspaper ads back in my State, saying, send these letters to Senator Metzenbaum. I feel so strongly about people involvement that I am always amazed that on some issues of maybe a far greater dimension and a far greater impact on the daily lives of people, they do not react at all. But in connection with this issue, there is a tremendous outpouring of people involvement. I think it is good for democracy, and it pleases me much. But having said that, let me address myself to the hearing itself, because I recognize it to be an important issue for the recording industry as well as for consumers.

And a real question is propounded as to whether it is fair for consumers to be able to tape record from the radio or from someone else's tapes or records for free, or should there be some compensation to the industry.

Now, it is certainly true that consumers in recent years have been able to tape record on high quality equipment. No doubt they sometimes decide not to buy a record or a cassette because they can make a recording. And if you can get it for nothing, why should you go out to the store and pay something for it?

The recording industry, therefore, may have some cause for complaint, and Congress should seriously consider the issues raised by the industry. But having said that, I am frank to say that I have some serious questions about this legislative proposal.

The industry proposes to tax consumers who buy tapes in the recording industry and then give the proceeds to the industry. Will talented but starving artists benefit from these royalties or will the big record companies and the better-known, well-known entertainers and performers like Michael Jackson and so many others, who earn millions of dollars a year already, end up with most of the money that would come from the proceeds of this piece of legislation?

The bill puts a tax on tapes of 1 cent per minute, or about $1 for a 90-minute tape. Now, I understand some 90-minute tapes sell for

$4 or less. If that were the case, there would be a 25-percent increase in the price that consumers must pay.

Now, having said that, I may sort of leave the impression that if the royalty were not that high, perhaps I would be more receptive to the legislation. But I have a basic question in my mind, and that is, should the consumers be called upon to pay this tax? And frankly, my mind has not resolved that issue.

Now, once the money is in, the bill allows the industry to get together to decide how to divide up the royalties, and it creates an antitrust exemption to allow them to do it. In my opinion, there is a very heavy burden on anyone who says they want to be exempt from antitrust laws, and that burden is not met here.

I find that more and more proposals in the United States propose to provide exemptions from the antitrust laws, whether it has to do with the beer industry or the football industry or the bottling industry or the shipping industry, or any one of a host of others, to the point where one has to be concerned as to whether or not the efficacy of our antitrust laws is being seriously effected.

The industry says it is losing money because of taping. That may be so, but the fact is that profits are up, and sales are up, and the industry certainly is not in financial trouble.

I look forward to hearing the testimony on the bill and the case that the recording industry makes, but I want to make sure that the consumer and consumer's interests are protected as we look at this legislation. And I will listen with bated breath as I listen to each of these witnesses and our congressional spokespersons who are here with us today.

Senator MATHIAS. Thank you very much, Senator Metzenbaum.

At this point, we will place into the record a statement by Senator Gore.

[Statement of Senator Gore follows:]

STATEMENT OF HON. ALBERT GORE, JR., A U.S. SENATOR FROM THE STATE OF TENNESSEE

MR. CHAIRMAN, DISTINGUISHED MEMBERS OF THE COMMITTEE, I WANT TO THANK YOU FOR THE OPPORTUNITY TO PRESENT MY VIEWS ON S. 1739, THE HOME AUDIO RECORDING ACT, OF WHICH I AM A CO-SPONSOR.

THIS IMPORTANT PIECE OF LEGISLATION IS THE RESULT OF THE CONSTANT CHALLENGE TO CONGRESS -- AND, IN FACT, TO THE ENTIRE AMERICAN GOVERNMENT -- TO KEEP THE LAW CURRENT WITH RAPIDLY CHANGING TECHNOLOGY. THE LAW AS IT NOW STANDS IS UNSETTLED ABOUT THE LEGALITY OF HOME TAPING. THIS IS THE CASE SIMPLY BECAUSE THE TECHNOLOGY FOR HIGH QUALITY STORAGE AND PRODUCTION HAS BEEN DEVELOPED FOR THE MASS MARKET ONLY IN THE LAST SEVERAL YEARS.

NEW TECHNOLOGIES MAKE HOME AUDIO TAPING OF FAVORITE MUSICAL RECORDINGS EASIER AND MORE ECONOMICAL. YET, AT THE SAME TIME, THESE ADVANCES MAKE IT MUCH MORE DIFFICULT TO PROTECT THE CREATIVE PROPERTY OF MUSICIANS, WRITERS, AND OTHERS WHOSE TALENT AND ENERGY ARE INVESTED IN THESE WORKS. THIS BILL IS PART OF THE ONGOING AND NECESSARY EFFORT OF CONGRESS TO DEVELOP THE LAW IN CONCERT WITH ADVANCES IN SCIENCE, COMMUNICATIONS, MEDICINE, AND OTHER AREAS OF RAPID HUMAN ACHIEVEMENT.

THIS EFFORT IS REQUIRED OF US NOT ONLY BECAUSE IT MAKES GOOD SENSE, BUT ALSO BECAUSE WE ARE CHARGED WITH THIS RESPONSIBILILTY BY THE CONSTITUTION. ARTICLE I, SECTION 8, MANDATES CONGRESS "TO PROMOTE THE PROGRESS OF SCIENCE AND THE USEFUL ARTS, BY SECURING FOR LIMITED TIMES TO AUTHORS AND INVENTORS THE EXCLUSIVE RIGHT TO THEIR RESPECTIVE WRITINGS AND DISCOVERIES...".

THE HOME AUDIO RECORDING ACT IS ESSENTIAL IF THIS POWER IS TO BE USED EFFECTIVELY TO PROTECT COPYRIGHT HOLDERS AND KEEP THE LAW OF COPYRIGHT CURRENT WITH DEVELOPING TECHNOLOGY. IT WOULD ESTABLISH THE LEGALITY OF A PRACTICE WHICH IS CURRENTLY WIDE-SPREAD -- THAT IS, THE HOME TAPING OF COPYRIGHTED MUSIC FOR PERSONAL USE FROM RADIO BROADCASTS, RECORDS, PRERECORDED CASSETTES, AND COMPACT DISCS. IT WOULD ENSURE THE DISTRIBUTION OF THE ROYALTY FEE IT IMPOSES TO THE COPYRIGHT HOLDERS, THOSE WHOSE TALENT AND WORK THE LISTENER ENJOYS.

IT IS ALSO IMPORTANT TO NOTE THAT S. 1739 IS CAREFULLY DRAWN TO ENSURE THAT NON-COPYRIGHT-INFRINGING MACHINES AND TAPES -- SUCH AS THOSE USED BY SCHOOLS AND BUSINESSES -- WOULD NOT BE SUBJECT TO ROYALTY PAYMENTS. EXEMPTIONS WOULD BE PROVIDED FOR BUSINESS DICTATION MACHINES AND TAPES AND OTHER EQUIPMENT UNSUITABLE FOR HOME TAPING. FINALLY, THE BILL ENCOURAGES TECHNOLOGICAL SOLUTIONS TO THE HOME TAPING PROBLEM BY EXCLUDING FROM ROYALTY FEES THOSE MACHINES WHICH ARE CAPABLE OF CONTROLLING TAPING OF CODED RECORDS AND PRERECORDED TAPES.

TESTIMONY BEFORE THE COMMITTEE WILL SUBSTANTIATE THE NEED FOR THIS LEGISLATION. HOME TAPING COSTS MUSICIANS, COMPOSERS, WRITERS AND OTHERS AS MUCH AS ONE-AND-ONE-HALF BILLION DOLLARS EACH YEAR IN LOST SALES. THOSE WHO CONTEND THAT THESE LOSSES ONLY AFFECT ALREADY-WEALTHY PERFORMERS AND RECORD COMPANIES REVEAL A FUNDAMENTAL MISUNDERSTANDING OF THE DIVERSITY OF THE MUSIC BUSINESS. FOR EVERY MICHAEL JACKSON WITH HIS SUCCESSFUL "THRILLER" ALBUM, THERE ARE THOUSANDS OF STRUGGLING SONGWRITERS AND MUSICIANS TO WHOM THE OFTEN MODEST ROYALTIES THEY RECEIVE MEAN THE CHANCE TO PURSUE A FULL-TIME CAREER IN MUSIC. THE MUSIC BUSINESS IS MADE UP OF A WIDE RANGE OF INDIVIDUALS -- SOME WEALTHY, AT LEAST THE FAMOUS ONES -- BUT MANY MORE WHO ARE SIMPLY MIDDLE-INCOME MEN AND WOMEN TO WHOM FAIR PAYMENT FOR THEIR WORK IS NOT SIMPLY A PRINCIPLE BUT AN ECONOMIC ESSENTIAL.

BUT PRINCIPLES ARE INVOLVED TOO. THE SIMPLE PRINCIPLE REPRESENTED BY S. 1739 IS THIS: IF YOU ENJOY ANOTHER'S PROPERTY -- INTELLECTUAL, ARTISTIC, OR OTHERWISE -- YOU SHOULD BE WILLING TO PAY FOR IT. THIS IS A FUNDAMENTAL CONCEPT WITH WHICH I BELIEVE THE VAST MAJORITY OF AMERICANS AGREES. I SUBMIT TO THE COMMITTEE THAT THE MUSIC FANS OF THIS COUNTRY DO IN FACT SUPPORT THIS PRINCIPLE, NOTWITHSTANDING A VERY SOPHISTICATED LOBBYING CAMPAIGN TO ASSERT OTHERWISE.

MUSIC FANS DON'T DEMAND FREE CONCERTS OR FREE ALBUMS; AND, ALTHOUGH THEY MAY BE TAKING ADVANTAGE OF FREE HOME TAPING WHILE THE LAW IS UNSETTLED, THERE IS LITTLE EVIDENCE THAT THEY CONSIDER IT AN UNALIENABLE RIGHT. THE AVERAGE MUSIC FAN

UNDERSTANDS THAT WHEN HE BORROWS A FRIEND'S ALBUM AND TAPES IT, RATHER THAN BUYING THE ALBUM HIMSELF, THE ARTIST DOES NOT RECIEVE JUST COMPENSATION FOR PROVIDING THAT ENTERTAINMENT. INDEED, UNDER THE CURRENT SYSTEM, NO MECHANISM EXISTS WHEREBY HOME TAPING FANS CAN COMPENSATE THE ARTISTS WHOM THEY ADMIRE.

THEREFORE, THIS LEGISLATION IS REALLY PRO-CONSUMER. IT GIVES MUSIC FANS WHO TAPE AT HOME A WAY TO COMPENSATE THOSE ARTISTS WHOSE WORK THEY ENJOY. AND THE CONSUMER WILL ALSO BE REWARDED WITH CONTINUED ACCESS TO A VARIETY OF RECENTLY RELEASED MUSIC.

AGAIN, I WANT TO THANK THE CHAIRMAN AND MEMBERS OF THE COMMITTEE FOR THE OPPORTUNITY TO TESTIFY. I URGE FAVORABLE CONSIDERATION OF S. 1739, AND I LOOK FORWARD TO WORKING WITH YOU ON ITS BEHALF.

Senator **Mathias**. Our first witness today is our colleague from the other body, Representative Bruce A. Morrison.

STATEMENT OF HON. BRUCE A. MORRISON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CONNECTICUT

Mr. **Morrison**. Thank you, Mr. Chairman.

First, I would like to commend you for scheduling this hearing and for introducing S. 1739. I am here to testify in favor of the bill and to discuss the reasons that I think this legislation and the companion bill that I have filed in the House, which is H.R. 2911, provide the basis for needed legislation in this area. The hearings that you have scheduled present an important opportunity, both for the Senate and for the House, to learn more about the problems caused by home taping and how to tailor legislation to protect the legitimate interests of consumers and copyright holders.

This is an attempt to achieve a balanced solution to a real problem—the problem of uncompensated taping of music both off the air and from existing prerecorded tapes, records, and discs. This unauthorized taping displaces large numbers of sales, thereby depriving owners of copyrights from compensation to which they are entitled.

It would be no real solution to this problem to try to outlaw this taping, although it is, at least arguably, already an infringement of the copyright and a violation of the law.

It would not be beneficial either to the industry or to the consumers to take that approach, but it is certainly fair and proper to expect that those who make copies of copyrighted materials for their own use would pay a fair royalty for that use. And that is what this legislation seeks to accomplish.

Much is said about the consumer interest in this area, and I certainly agree with Senator Metzenbaum that the consumer interest should be respected. But consumers do not have the right to have something for nothing. Consumers have a right to a fair price, but they also have a responsibility to pay for that which they consume.

The copyright laws exist for the benefit of consumers in the long run. They benefit consumers by promoting the production of the broadest and the most diverse array of creative materials. It is important that Congress not shy away from the challenges posed by the kind of technological change which we have seen in this area in terms of the easy availability of taping equipment. It continues to happen throughout the copyright area and Congress must be flexible and able to respond to these changes, continuing to balance the interests of the consumers to access and the producers to fair incentives to produce.

It seems to me that the opposition to this kind of legislation that I expect the committee will hear from the producers of recording equipment is shortsighted. Certainly, their entire business is based on the broadest availability of taped materials on the air and available for sale, and in many ways they share the same interest as the producers.

In the long run the health of the music industry, the breadth of the offerings that are available, will make their goods that much more attractive, especially since this legislation does not seek in any way to ban taping. Those who produce tapes really do not have a contrary interest and ought to be working with the committee to try to forge the best possible bill to promote an interest I think we have in common.

Let me just speak for a moment about the similarity between H.R. 2911 and S. 1739. They seek to accomplish the same goal and use the same general approach. A per-minute royalty on the blank tapes and a percentage royalty on taping equipment, with a higher royalty to be charged on the dual cassette recording media, since they are much more likely to be used for duplicating taping. There is a difference between the two bills in the amount of the royalty on the single-deck cassette.

My bill proposes 10 percent on the wholesale price, and your bill, Mr. Chairman, proposes a 5-percent royalty. It seems to me that setting an appropriate level for the royalty is one of the things that the hearing and deliberation process needs to look at. This should be a fair compensation scheme. It should not be an attempt to impose an excessive cost that will make it difficult or impossible for people to tape.

I believe that these bills, both your bill in the Senate and my bill in the House, should and will gain widespread support as their purpose and technique is understood more fully. And I once again commend you for having filed the bill and also having scheduled these hearings, so we can learn more about how to actually implement what I think on its face is a very good idea.

Senator **Mathias**. Thank you very much, Mr. Morrison.

Do you have any questions, Senator?

Senator **Metzenbaum**. No, I do not. It was an excellent statement.

Senator **Mathias**. Thank you very much for being with us.

Senator DeConcini has joined us.

OPENING STATEMENT OF HON. DENNIS DeCONCINI, A U.S. SENATOR FROM THE STATE OF ARIZONA

Senator **DeConcini**. Mr. Chairman, I apologize for my tardiness. My statement is indeed short. We are once again considering legislation that would require the American music consumer to pay a fee on blank cassettes for cassette recorders.

As you know, the subcommittee has had many hearings over the last 4 years on the general issue of technological advances in electronics in the entertainment industry, and how our copyright laws should be adjusted to cope with those advances.

In my opinion, on the whole, our system of copyright has adjusted well to these advances. Absent clear and convincing evidence to the contrary, I do not believe our copyright laws are in need of any major adjustment.

I will review the testimony presented here today. I have to go to an appropriations conference committee in about a half an hour. I will not be able to stay for the full hearing.

If the proponents are able to produce evidence that a fee arrangement is appropriate, I will be certainly happy to participate in the discussion of the amount of such a fee, and on what material it ought to be applied.

I am greatly concerned, just by looking at the bill, that we are talking about 1 cent per minute. This seems to me to be a very, very large fee, but nevertheless, Mr. Chairman, I thank you for holding these hearings and the continued fairness and total openness with which you have permitted the witnesses to testify. And I look forward to watching these hearings very carefully.

Senator **Mathias**. Our next witness is the Honorable Ralph Oman, Register of Copyrights, Library of Congress. The Chair will take this opportunity to note that this is the first time that Mr. Oman has returned to the subcommittee since he left as its chief counsel. He comes in his new position as Register of Copyrights, and we are very happy to have him.

Mr. Oman, would you introduce your associates.

Mr. **Oman**. Mr. Chairman, on my right is the general counsel of the Copyright Office, Dorothy Schrader, and to my left is a senior attorney in the general counsel's office, Marilyn Kretsinger.

Senator **Mathias**. We are happy to have them back with us.

STATEMENT OF HON. RALPH OMAN, REGISTER OF COPYRIGHTS, LIBRARY OF CONGRESS, WASHINGTON, DC, ACCOMPANIED BY DOROTHY SCHRADER, GENERAL COUNSEL, COPYRIGHT OFFICE, AND MARILYN KRETSINGER, SENIOR ATTORNEY, GENERAL COUNSEL'S OFFICE

Mr. OMAN. It is nice to see many familiar faces and old friends, and I should observe that I have been beyond the dias, and now I am in front of the dias, and I think back there is better.

Mr. Chairman and members of the subcommittee, I am pleased to make my first appearance in a congressional hearing as Register of Copyrights before this distinguished body. Thank you and the subcommittee staff for the opportunity to appear here today and testify on S. 1739, the Home Audio Recording Act.

It is my hope as Register that the Copyright Office will continue the tradition of providing objective technical support to the lawmaking process.

Because of my own personal involvement in helping you draft the bill when I worked on your subcommittee, Mr. Chairman, I will only comment generally on the underlying position of the Copyright Office, and Ms. Schrader will respond to questions that deal specifically with the bill.

Your consideration of S. 1739 is a timely one.

Ten countries have already enacted legislation that places a royalty or tax on taping equipment and media. France became the 10th country to do so only this year. Nine of these countries have acted on this issue within the past 5 years. More and more countries are considering legislation to compensate copyright proprietors for home taping.

The new bill builds on the earlier bills, but it has several changes that better accommodate the interests of consumers, copyright proprietors, and arguably, the manufacturers of the machines and blank tape. Providing an exact fee schedule eliminates a great deal of uncertainty and makes the fixing of royalties less cumbersome. The separation of audio from video recording also makes this bill more palatable. If the subcommittee decides to move the bill, the definitions should be amended, to make certain that the royalty is only on tapes or recorders that are used primarily for audio recordings—or in the alternative are not capable of also making video recordings. The amount of the royalty would also be another area for closer scrutiny.

The new bill goes farther than its predecessor—S. 31—in setting out exemptions for noninfringing uses, in response to the Audio Recording Rights Coalition [ARRC] argument that millions of consumers would be penalized for taping that is unrelated to copyrighted music. Unlike the House bill, the Senate bill entrusts to the Copyright Royalty Tribunal the regulation of noninfringing uses and distribution of royalties.

It is clear from the testimony of the Recording Industry Association of America and ARRC that they are unable to come to any voluntary agreement. Therefore, a legislative solution is called for, if Congress deems compensation for home audio recording appropriate. Congress is the lawgiver, and the branch of Government that best balances the equities and formulates a comprehensive remedy that binds all parties, as the Supreme Court stated in *Sony Corporation of America* v. *Universal City Studios, Inc.*

You've heard all the arguments, pro and con, and I won't repeat them here. My prepared statement recounts that familiar history.

Instead, I will make some general observations about home taping as a copyright problem. Some of the witnesses today will argue that the failure to enact this bill immediately will spell doom for American creativity. Other witnesses will offer grave predictions that enactment of this bill will mean the brutal exploitation of consumers by rapacious copyright owners.

The question is not so much whether or not anyone will be hurt by S. 1739, but whether or not, on balance, S. 1739 promotes the purposes of the constitutional provision.

Last year, Congress passed the record rental amendment. That act effectively prohibits the commercial renting of records and tapes. Now, there were no doubt some very sincere people whose only interest was listening to the records and returning them. They had no interest in taping the record, but Congress had to balance this fact with the evidence that record rental was by and large a subterfuge for home taping operations. So Congress stepped in and stopped it. That action was unfair to the people who only wanted the innocent pleasure of listening to the music on the record, but Congress had to respond to the overwhelming evidence, and their rights were brushed aside.

In the same way, Congress could decide that, on balance, a royalty on blank tape and machines is the way to solve the home taping problem. You could find the cost small in relation to the benefit.

If the evidence is persuasive, but not overwhelming, you might want to consider a sunset provision. The record rental amendment has such a provision.

Perhaps, 3 to 5 years after enactment, you might want a careful review of the national experience on whether creative and user environments have been helped or harmed by a home taping law. These are possibilities that the Copyright Office would be pleased to address in a written submission to the subcommittee if you so desire.

The Office is also ready to help you examine the testimony given today and to evaluate the studies that have been prepared, among them the OTA study that is due at the end of the year. All things considered, S. 1739 is a distinct improvement over bills considered in previous congresses. Further finetuning will naturally occur, especially on the role of the Copyright Royalty Tribunal in its implementation. But, overall, the bill is technically sound.

Like all other copyright measures, it should be tested against the constitutional purpose: Is compensation to copyright owners for home audio recording likely to invigorate creative instincts, and encourage the creation and wide dissemination of the works thus created? In the long term, will public benefit from the availability of new creative works outstrip the added cost to the consumer of audio recording devices and media? That is a judgment for the Congress to make on behalf of the public as a whole.

Thank you. Ms. Schrader and I will be pleased to respond to any questions.

[Mr. Oman's prepared statement follows:]

PREPARED STATEMENT OF RALPH OMAN

Register of Copyrights and
Assistant Librarian for Copyright Services

Before the Subcommittee on Patents, Copyrights and Trademarks
Senate Committee on the Judiciary
99th Congress, First Session
October 30, 1985

Mr. Chairman and members of the Subcommittee, I am pleased to make my first appearance in a congressional hearing as Register of Copyrights before this distinguished body. Thank you and the Subcommittee staff for the opportunity to appear here today and testify on S. 1739, the Home Audio Recording Act.

As you noted on October 7, 1985, Mr. Chairman, when you introduced S. 1739, this bill addresses the problems caused by "the unrestricted home taping of copyrighted music." Although S. 1739 is not unlike its predecessor, S. 31, introduced in the 98th Congress, several significant developments have occurred on both the domestic and international levels since that bill was introduced. You appear to have taken all of these developments into consideration in your new draft.

Introduction

In many ways S. 1739 is similar in approach to the legislation introduced in the 98th Congress (S. 31; H.R. 1030). Unlike earlier bills, however, S. 1739 only addresses the issue of home audio recording. It provides for the amendment of title 17 of the United States Code with respect to home audio recording and audio recording devices and media. The proposed legislation requires manufacturers to have a compulsory license to distribute their products in the United States and places a royalty on blank audio tape and audio recording equipment in order to compensate the copyright owners whose works are being reproduced.

The subject matter of S. 1739 is not a new one on the national 1/ or international level; it addresses a problem that is receiving world-wide attention as recording companies and copyright owners continue to urge that the proliferation of home taping results in massive losses to the recording industry each year. Consequently, home taping has been examined on the international level through joint studies made by the World Intellectual Property Organization (WIPO) and the United Nations Educational, Scientific and Cultural Organization (UNESCO) and also on the domestic level.2/

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1. Home taping bills were also introduced in the 97th Congress.

2. See App. I for a partial listing of these studies.

The timeliness of S. 1739 is emphasized by the fact that when France recently enacted copyright legislation placing a royalty on taping equipment and media, it became the tenth country to provide for some kind of compensation. Nine of these countries have acted on this issue within the past five years. Even as you decide whether or not to enact S. 1739, several other countries are considering similar legislation.3/ Within the past few years, virtually, all industrialized countries have wrestled with the problem of how best to compensate copyright proprietors without unduly restricting home taping.

As you know, its supporters argue that this royalty will to some extent compensate copyright proprietors for the making of uncompensated and unauthorized reproductions. The Recording Industry Association of America (RIAA) claims that the industry loses one and one-half billion dollars annually in U.S. sales alone. Recording industries within other countries also report substantial losses. Copyright proprietors urge that their talents and their work are responsible for the phenomenal business enjoyed by the manufacturers and importers of audio recording devices and media. Consumers,

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3. Austria, the Congo, Finland, Hungary, Iceland, and the Federal Republic of Germany have a royalty. Three other countries, Norway, Turkey, and Sweden, have a tax. Billboard, July 13, 1985, at 9. Holland is expected to place a levy on audio and video tapes and hardware by the end of this year. Billboard, Aug. 31, 1985, at 13. The Canadian Subcommittee on the Revision of Copyright has recommended a royalty for home taping on both the media and the recording devices. Denmark, Italy, the Netherlands, Switzerland, and the United Kingdom are considering legislation. A Charter of Rights for Creators, Canada House of Commons: Report of Subcommittee on the Revision of Copyright 74-76 (Oct. 1985).

manufacturers, and retailers respond that the recording industry is healthy today and that any problems in the past were not due to home taping. They also assert that the recording industries' prosperity is in many ways the result of the new technologies developed by the manufacturer which have created a whole new market for copyrighted media.

Of course we can't examine S. 1739 in a vacuum; we should also examine the extent of home taping of copyrighted music, look at the equities involved in this taping, and evaluate the methods available if compensation of copyright proprietors is desired. It is only through this kind of evaluation that we can determine whether or not Congress can resolve the home audio taping question within this country in an unobtrusive way that serves the needs of consumers, copyright proprietors, and the importers, manufacturers, and distributors of the audio devices and media.

I. THE LEGISLATIVE BACKGROUND

A. Legislative History of Home Taping Bills.

In 1982 a number of home taping bills were introduced in the 97th Congress. Several bills (S. 1758, H.R. 4783, H.R. 4794) exempted home video recorders from copyright liability whenever copies were made for private noncommercial use. Amendment 1333 to S. 1758 and H.R. 5705 provided an exemption for both audio and video recording but based this exemption on the payment of royalties on both the recording devices and the blank tapes used to make the copies. These later bills (Amendment 1333 to S. 1758 and H.R. 5705) attempted to resolve all of the problems related to home taping in one package.4/ Hearings were held on the home taping bills introduced in the 97th Congress in both the House and the Senate.5/ A great deal of attention was also given to these issues in the press, especially since the Supreme Court was preparing to hear the Betamax case.6/

One might have expected the bills introduced in the 98th Congress to reveal compromises to accommodate the divergent views presented in the 97th Congress; however, a blanket exemption was again proposed in both houses. H.R. 175 (S. 175) exempted home video recorders from copyright liability whenever the copies made were for private noncommercial use. It did not reach audio home recording. Proponents of protective measures introduced: S. 31 (H.R. 1030) which covered both home video and audio recording devices and media and was referred to as the Home Recording Act of 1983; S. 32 (H.R. 1027) which covered

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4. Section 5 of Amendment 1331 to S. 1758 also would have created a commercial lending (rental) right in motion pictures and other audiovisual works and sound recordings, by narrowing the scope of the present "first sale" limitation on the public distribution right.

5. See, App. II for a list of the Bills introduced, the Hearings that have been held and the Reports that have been issued in both the 97th and 98th Congresses.

6. This case was not settled by the Supreme Court until 1984, see, Sony Corporation of America v. Universal City Studios, Inc., 464 U.S. 417 (1984), rev'g Universal City Studios Inc. v. Sony Corporation of America, 659 F.2d 963 (9th Cir. 1981), rev'g 480 F.Supp. 429 (C.D. Cal. 1979).

the rental, lease, or lending of sound recordings; and S. 33 (H.R. 1029) which covered the rental, lease, or lending of motion pictures and other audiovisual works.

Although the 98th Congress did not pass any legislation that covered home taping, it did pass the Record Rental Amendment (S. 32, H.R. 5938). This bill became law on October 4, 1984. Pub. L. No. 98-450, 98 Stat. 1727 (1984).

In the 99th Congress H.R. 2911 and S. 1739, bills concerned with home audio taping, have been introduced. No bills, neither blanket exemptions nor protective measures, have been introduced in the Senate dealing with video home recording.

B. Comparison of S. 1739 and S. 31 [7]

A cursory examination of the current audio home recording bill with its predecessor reveals three major differences: (1) S. 1739 would legislate a specific rate of royalty while S. 31 provided that the compensation was to be determined by voluntary negotiation or, as a last resort, compulsory arbitration; (2) S. 1739 introduces new definitions and language that covers recent technological developments; and 3) S. 1739 addresses only home audio taping. Nevertheless, a

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7. S. 31, introduced in the Senate on January 26, 1983, is identical to H.R. 1030, introduced in the House on January 27, 1983.

comparison of the two bills reveals that the underlying structure and many of the provisions are quite similar. In fact a great deal of the language is identical.

C. Basic Features of S. 1739.

1. Limitation on Liability: Audio Recording [§119(a)]. S. 1739 omits the preamble that summed up the congressional power to give authors an exclusive right and discussed the value of this system, the role of home recording devices and media, and the policy reasons behind the legislation that permitted the home recorder to tape upon the payment of compensation.8/ However, some of the same material can be found in other parts of S. 1739.

S. 1739 contains a section that sets out the limitation on liability for home audio recording, which begins with an exemption for individual taping. S. 1739 then states:

> [N]othing in this section shall exempt from liability a person who, for purposes of direct or indirect commercial advantage, induces, causes or materially contributes to the making of audio recordings by any individual or entity.

(§119(a)).9/

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8. Both S. 31 [§120(a)] and its predecessor contained such a preamble. See §120(b).

9. This provision complies in purpose with the directive in the S. 31 preamble that there will be no direct liability on the individual who tapes for private purposes. (Section 2(i).)

2. Compulsory License [§119(b)]. S. 1739 establishes a compulsory licensing scheme.10/ This scheme provides that in order to get a compulsory license and thus escape liability for copyright infringement an importer or manufacturer of any recording device or medium must record a notice and deposit a statement of account and the specified fee with the Register of Copyrights. The notice which contains business information as prescribed by regulation must be recorded one month before distribution for any audio recording device or medium.11/ The statement of account gives the number of audio recording devices or amount of audio recording media imported into or manufactured in the United States, the number or amount distributed in the United States during the preceding period, and any other information prescribed by regulation. This statement is to be accompanied by the total royalty fee specified. There is one important change in this section: S. 1739 specifies royalty rates.12/

3. Infringement [§119(b)(2)(A) and Remedies for Infringement [Sec. 3]. S. 1739 provides that the importation into and distribution in the United States, or the manufacture and distribution in the United States, of any audio recording device or audio recording medium is actionable as an act of infringement under the pertinent provisions of chapter 5 of the

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10. The language used to describe this scheme is almost identical with that found in S. 31. §120(b).

11. Or within sixty days after the effective date of this Act, whichever is later.

12. S. 31 specifies a negotiated or arbitrated fee.

Copyright Act if the notice, statement of account, or total royalty fee specified has not been recorded or deposited, or if the statement of account or total royalty fee does not materially comply with the requirements of paragraph (1) or any regulations prescribed thereunder.13/

A major change in this subsection is that S. 1739 places the importation and distribution or manufacture and distribution of "multiple audio recording devices"14/ outside the compulsory license and makes such importation, distribution, and manufacture immediately actionable.

S. 1739 amends chapter 5 of title 17 by inserting a new section.15/ The new §511 gives an additional remedy for infringing importation or manufacture, and distribution of audio recording devices or media. Under this section a court may deprive the manufacturer or importer of the benefit of the compulsory license for up to 90 days. Without a license the importation and distribution or manufacture and distribution during the deprivation period would be actionable under §501 and subject to the remedies set out in sections §§502-506, §509, and §511.

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13. S. 31 made the failure to record or deposit actionable if it was willful or repeated. §120(b)(2).

14. A "multiple audio recording device" is defined as one "... which contains in a single apparatus one or more cavities for the insertion of a phonorecord in any such format and two or more cavities for the insertion of an audio recording median in any such format." §119(d)(6).

15. This amendment is also found in S. 31. [Sec. 4].

4. Royalty Fees [§119(c)], Exemptions [§119 (c)(1)(D), (E)], and Adjustments [§119(c)(2)(B)]. S. 1739 sets out a specific royalty fee.[16] Subsection 119(c) establishes a fee that is 5% of the price charged for the first domestic sale[17] on each audio recording device imported into and distributed in the United States or manufactured and distributed in the United States. The royalty on dual audio recording devices[18] is 25% of the price charged for the first domestic sale. The royalty on an audio recording medium is one cent per minute of the maximum playing time or fraction thereof.

The statute specifies that the royalty is placed on equipment or tapes used to make "audio recordings." Some video recorders and cassettes are now being used to make "audio recordings," *i.e.*, only the sound track portion of the tape is used. It seems appropriate, therefore, to redraft the definitions found in §119(d) to clarify that only those recorders and tapes which are made primarily for audio use fall under this compulsory license.

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[16] S. 31 provided for a determination of fees by voluntary negotiation or arbitration. §120(c).

[17] "The 'first domestic sale' of an audio recording device is the first sale of such device in the United States to an unrelated party. For purposes of this paragraph, an unrelated party is a person who is not controlling, controlled by, or under common control with the seller, and who is not acting in concert with the seller in order to avoid or lessen the obligations of subsection (b). Control will be deemed to exist if there is a fifty per centum or greater direct or indirect ownership interest between the seller and such other person." §119(d)(5).

[18] "A 'dual audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one cavity for the insertion of a phonorecord in any such format and one cavity for the insertion of an audio recording medium in any such format." §119(d)(4).

S. 1739 also contains a more detailed explanation of uses that may not be subject to the payment of royalty fees.19/ It permits the Copyright Royalty Tribunal (CRT) by regulation to exempt devices or media unsuitable for such recording, and also to establish a procedure for the exemption of devices or media when any part of the purchase price is deductible under §162 or depreciable under §167 of the Internal Revenue Code of 1954 or where the devices or media are not to be used for infringing acts.

S. 1739 provides for the adjustment of the royalty fees specified by the CRT in the fifth calendar year and every subsequent fifth year after the fee section becomes effective.20/ The CRT is to be guided in its determination of fee adjustments by ten criteria that attempt to balance the equities.21/

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19. S. 31 provided that during the voluntary negotiations to determine fees, voluntary agreement could distinguish different kinds of devices or media and exempt those that are used substantially all of the time for other purposes than making audio recordings in private homes. §120(c)(3)(E).

20. S. 31 provided for an adjustment of royalty fees through commencing an arbitration proceeding every third year. §120(c)(6).

21. These are almost identical to the criteria that were to guide the Arbitration Board in determining royalty fees under S. 31. [§120(c)(3)(D)] S. 1739 adds one new criterion, "new technologies for making audio recordings

5. Deposit [§119(b)(3)] and Distribution of Royalty Fees [§119(b)(5)] to Copyright Owners [§119(b)(4)]. S. 1739 provides that the royalty fees are to be deposited with the Register who shall deduct reasonable administrative costs and deposit the remainder with the United States Treasury who will invest the royalty fees in interest bearing securities. The fees and interest are to be distributed by the CRT. The Register shall give the CRT a compilation of all statements of account covering the pertinent periods, and the Register and Secretary of Treasury are required to maintain separate and distinct accounts and records for fees deposited pursuant to this subsection.22/

It also provides that the copyright owners entitled to royalty fees are the owners of copyright in musical works and sound recordings included in radio or television transmissions, or distributed to the public in the form of phonorecords during the period which royalty fees cover.23/

Every person claiming to be entitled to a share shall file a claim for fees with the CRT as prescribed by regulations issued by the CRT. Without any fear of an antitrust violation, any claimants may agree among themselves as to the proportionate division of these fees, may lump their claims together

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by individuals for private use." It also eliminates the references to voluntary negotiation, the structure and financial condition of the music and recording industries, and reasonable estimates of the use of the devices or media for other purposes, that were found in S. 31.

22. S. 31 is identical. §120(b)(3).

23. See, S. 31, §120(b)(4).

and file them jointly or as a single claim or may designate a common agent. The CRT also determines whether there is a controversy concerning the distribution of royalty fees. If there is no controversy, the CRT distributes the fees after deducting reasonable administrative costs. If there is a controversy, the CRT conducts a proceeding, pursuant to chapter 8 of title 17, to determine the distribution of royalty fees. During such a proceeding, the CRT has discretion to distribute only those fees not in controversy.24/ Judicial review of this determination is already provided for in 17 U.S.C. §810.

II. THE AUDIO HOME TAPING DILEMMA

A. Extent of National and International Audio Home Taping (Private Copying).

As discussed earlier the home taping of music is causing considerable concern within the international recording industry. Audio taping became much more feasible in the mid-1960's with the development of cassette tape recorders which made audio taping both easier and less expensive.25/ Since the early 70's national and international organizations have commissioned surveys to measure both audio and video home or private copying.26/ Thus, it is possible today to examine

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24. The same distribution procedure was found in S. 31, §120 (b)(5).

25. Electronic Industries Association, Consumer Electronics Annual Review 33 (1985).

26. *See* App. I for a partial listing of those studies.

these surveys and make some observations about the extent and effects of either audio or video home taping on the national and international level.

Since about 1973 the International Federation of Producers of Phonograms and Videograms (IFPI), their affiliates, and other interested organizations, have collected statistical data. In 1982 IFPI released a report on home taping in six countries based on these surveys of audio home taping and other statistical material. This report revealed that the percentage of households with at least one tape recorder was very high within these countries:

Country	Households With Audio Recorders	Date Applicable 27/
Austria	40%	September 1974
France	37%	March 1979
Federal Republic of Germany	60%	April 1978
Japan	87%	August 1978
United Kingdom	56%	January 1980
United States	48%	June 1980 28/

This report also gave estimates of the blank tape29/ sales within these countries for the most recent year available at the time the report was made:

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27. The last column indicates the date of the information reported for a particular country.

28. 18 Copyright, 226 (July-August, 1982).

29. This survey includes cassettes, 8-track cartridge and reel-to-reel tapes.

Country	Date Applicable	Blank Tapes Sold (Million Units)
Austria	1981	30
France	1981	42
Federal Republic of Germany	1981	80-100
United Kingdom	1980	71
United States	1980	344 30/

As revealed in more recent studies, the penetration of audio tape recorders is not only much higher today but continues to grow each year in every country surveyed. A 1983 study, prepared at the request of the Council of Europe, reported that all of the countries within the European Economic Community (EEC) had a household penetration level of above 60%, with the United Kingdom showing the highest percentage, 73%, and the Nordic countries next with about 70%.31/ The report gives new figures for four of the six countries included in the 1982 IFPI report; these new figures reveal an increase in the sale of blank audio cassettes.

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30. 18 Copyright 226, 227 (July-August, 1982). This report has no data on this point for Japan.

31. IFPI, Private Copying of Sound and Audio-Visual Recordings 18-19 (1983) (Council of Europe Study). This report was prepared at the request of the Council of Europe to supplement an earlier report prepared by Gilian Davies also entitled, Private Copying of Sound and Audio-Visual Recordings prepared at the request of the Commission of the European Communities (hereafter EEC study) (1984). The Davies study covered only countries within the EEC; the second study added the non-EEC Member states of the Council of Europe.

Country	Date Applicable	Million Units
Austria	1982	9.0
France	1982	44.0
Federal Republic of Germany	1982	108.0
United Kingdom	1981	73.4 32/

The Council of Europe study reports that other European countries where surveys have been made reveal similarly high penetration levels for audio recorders and that in countries where successive surveys have been made there is a widening gap between the purchase of prerecorded and blank cassettes.33/ Figures released by the Electronic Industries Association (EIA) reveal growth in the sale of audio recorders and blank tapes in the United States during the last five years.34/

Year	Audio Recorders 35/	Blank Audio Tape 36/
1980	19,532,000	
1981	22,475,000	201,439,000
1982	20,201,000	186,447,000
1983	21,189,000	241,277,000
1984	24,705,000	254,798,000

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32. *Id.*, Council of Europe Study, Annex 3.

33. *Id.* at 19.

34. Electronic Industries Association, *Consumer Electronics Annual Review* 33-34 (1985). The latest figures released by ITA only reveal a 1.3% increase in 1984 in the sale of blank audio cassettes, but there were 243 million units sold during this period. *Variety*, July 10, 1985, at 1.

35. *Id.* at 33. These figures represent the imports of audio recorders.

36. *Id.* at 34. These figures represent sales to dealers.

B. Ensuing Copyright Problems and the Equities Involved.

Surveys reveal that almost every household in America has an audio tape recorder,37/ and IFPI has reported that the overwhelming majority of the material recorded on blank audio cassettes is music.38/ Potentially, therefore, home audio taping exploits a copyrighted work without compensating the copyright proprietor.39/ Of course, making a tape is not the same calculated theft of copyrighted products as piracy, but it is equally true that when someone makes a copy of a copyrighted audio work, there is no need to purchase the same work from the copyright proprietor. Thus, at least a potential sale may be lost. In the past surveys have revealed a decline in the sales of prerecorded music.40/ The most recent figures released show that sales are up for the past year but profits are down, and RIAA claims that home taping is partially responsible for lost profits.

It is, of course, impossible to determine how much of the past revenue loss is due to home taping. It is possible, however, to predict that home taping will increase especially

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37. IFPI suggests that home taping is high even in those countries where no surveys have been made.

38. See 18 Copyright 226, 227 (July-August 1982). This is borne out by later surveys.

39. See generally, Masouye, "Private Copying: A New Exploitation Mode for Works," 18 Copyright 81 (Feb. 1982); Fiscor, "The Home Taping of Protected Works: An Acid Test for Copyright," 17 Copyright 59 (Feb. 1981).

40. There has been a decline in sales in the United States and in other countries. See Fig. 5, EEC Study; Annex 2, Council of Europe study, supra note 31.

in those countries where the price of the prerecorded product is extremely high. Although there is no exact measurement of the loss of profits due to audio home taping, the yearly sales increases in every country surveyed for both audio equipment and blank tapes indicates that there have been and will continue to be substantial losses to the recording industry due to home taping.41/

Taping is commonplace, and most tapers either do not realize or would not admit there is any wrongdoing involved in this activity. Thus, it is not surprising that tapers have joined consumer groups to protest any royalty or levy on home taping.

The Audio Recording Rights Coalition (ARRC)42/ responds to RIAA by urging that American consumers have been lawfully engaged in the practice of home audio taping for their own personal enjoyment for twenty-five years. It claims that the recording industry is now enjoying record-high revenues and profits and that any past difficulties were not due to home taping. ARRC asserts that current recording profits are

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41. For example if the 90 million blank tapes sold in Germany in 1977 were sold as prerecorded tapes at DM 15.00 per tape the additional sales would have amounted to DM 1.35 billion. The portion of this retail price of DM 15.00 that would have gone to authors and performers would have been DM 3.00 per tape, but the fee on tape recorders generated only DM 15 or approximately 6 cents per blank tape sold. Seemann, "Sound and Video-Recording and the Copyright Law: The German Approach," 2 Cardozo Arts and Entertainment L.J. 225, 252-3 (1983). See also, the Council of Europe study, supra note 31, at 23.

42. The ARRC is made up of Japanese and American manufacturers of consumer electronics and blank tapes, retailers, and consumers.

partially due to the success of new equipment from the electronics industry and losses are partially due to industry mistakes. It also notes that its survey reveals that the taping of prerecorded music accounts for less than one-half of all audio taping.43/ ARRC reports that it is the taper who buys more records than any other consumer group and that more than half of the recordings made are from records the taper has already purchased. ARRC urges that this royalty would ultimately be passed on to the consumer.

Thus, there is not only a heated controversy as to the amount of taping of copyrighted music, but the annual loss to the recording industry due to home taping is equally disputed. Undoubtedly, there are equities on both sides, but in the furor raised by the dialogue between these groups, it is sometimes easy to lose sight of the real issue. Should the copyright law provide compensation for copyright proprietors for unauthorized reproduction of copyrighted works?

While the general consensus among copyright proponents is that copyright proprietors should be compensated for home taping of copyrighted works, the opponents of such measures have produced some viable arguments. One of these is the question of whether copyright is a property right or a statutory right and whether copyright owners are entitled to all earnings or only nominal compensation.44/ Another

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43. RIAA counters that the ARRC survey measured taping occurrences instead of uses and that the taping of an entire album would only be considered one occurrence.

44. See Selsky, "Is Copyright a Property Right or a Creation

important consideration is how equitable are royalties in general and these royalties in particular.[45] As opponents observe, any collection of royalties for recording copyrighted music seems more equitable if it goes directly to the composer or performer of copyrighted music being taped. This kind of distribution is not always possible.[46]

C. Alternative Solutions to Home Taping.

The 1982 IFPI report argued that there was a need to compensate copyright owners for home taping, pointed to national and international efforts to provide such compensation, and urged that only through national legislation such as that already enacted in Austria and the Federal Republic of Germany could such remuneration be made.[47] International copyright groups such as UNESCO and WIPO have also begun to study home taping's effects on copyright proprietors, to look for solutions within the international conventions, and to encourage national legislation. In the last five years many countries have begun to explore ways to provide compensation for unauthorized and unrestricted home taping.

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of Statute?" Entertainment and Sports Law, Spring 1984 at 14, cited in Comment, "Home Audio Recording After Betamax: Taking a Fresh Look," 36 Baylor L. Rev. 855, 857 at note 16 (1984).

[45] Berger, "The Dubbing Debate: How Fair Would the Tape Tax Be?" 1 Audio Review 1 (October, 1985).

[46] *See* text *infra* for a discussion of distribution schemes.

[47] *See*, 18 Copyright 226-231 (July-August, 1982).

1. Legislative Solutions. Several countries have legislated systems which require blank tapes to be marked, usually with a stamp or tag available upon payment of a fee by the manufacturer or importer, before they can be put on the market.48/ Seven countries have passed legislation providing for a royalty on taping equipment and media, and three other countries provide for a tax.

a. Stamp or Tag. The UNESCO/WIPO report indicates that Greece and some other countries have legislation that requires blank tapes to be marked by a tag or stamp (in reality a fee). It does not indicate how this system works.49/

b. A royalty or levy. This form of compensation has been called a levy under copyright law and described as "an obligation under private law requiring certain persons, mainly manufacturers or importers of certain materials, to pay a levy to the owners of rights or their organizations."50/ Seven countries--France, the Federal Republic of Germany, Austria, Hungary, the Congo, Finland, and Iceland--now place a royalty on blank tapes and several of them place a royalty on recording equipment as well.

In 1965 the Federal Republic of Germany became the first country to pass legislation calling for the payment of a royalty or levy of up to five percent of the proceeds by the

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48. Secretariats of Unesco and WIPO, Unauthorized Reproduction for Private Purposes of Sound and Audiovisual Recordings, Broadcasts and the Printed Word 34 (June 4-8, 1984).

49. Id. at 34.

50. Id. at 17.

"manufacturer of equipment suitable for making such reproductions." Collecting societies within the field formed a joint association ZPU (Zentralstelle fur private uberspielungsrechte) to facilitate administration of this remuneration. In 1981 thir~~ty-nine~~ million deutschmarks was collected under the FRG provision.

Collection of anticipated royalties under the 1965 German provision proved to be quite unsatisfactory:

1. The negotiated fee proved to be slow and cumbersome, and the 5% ceiling was never reached.
2. The retail price on audio recorders dropped sharply after the 1965 law was enacted and continued to decline.
3. The audio recorder market was stagnant by the late 1970's since almost every German household had a recorder.51/

On June 24, 1985, the German Parliament amended the 1965 Copyright Act. Article 54(1) now calls for remuneration on both the equipment and the tapes (videograms or phonorecords). Article 54(5) permits authors to demand sales figures from manufacturers and importers so that levy revenues can be determined, and the annex to 54(4) sets a specific remuneration rate. The rate for each sound recording device is DM 2.50, and the rate for phonorecords for each playing hour in

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51. Seemann, "Sound and Video-Recording and the Copyright Law: The German Approach," 2 Cardozo Arts and Entertainment L.J. 225, 249-253 (1983).

ordinary use is DM 0.12. 52/ Thus, the new provision addresses all of the problems in the 1965 law.

On July 2, 1980, Austria passed copyright legislation that placed a levy on blank tapes. The money is to be distributed by Austrian collecting societies. In 1981 this levy produced about six million Austrian schillings. The rates were raised on January 1, 1982, to 2.25 schillings/hour of playing time.53/

On November 20, 1982, Hungary passed a law providing for a levy on blank recording material of 8% of the returns or sales. The law also specifies how the money is to be distributed among the copyright proprietors.54/

On July 7, 1982, the Congo passed a law providing for a payment to the author based on a percentage of the sale of blank mediums.

Since the completion of the WIPO report three other countries,55/ France, Finland, and Iceland, have provided similar levies on taping media and/or equipment, and other countries are considering similar legislation.56/

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52. The current exchange rate is 2.64 DM to $1.00 (October 23, 1985).

53. UNESCO/WIPO report, supra note 48, at 18. The current exchange rate is 18.48 Austrian schillings to $1.00 (October 23, 1985).

54. Id. at 18-19.

55. Id.

56. See, Appendix III for a comparison of the royalty schemes in these countries.

The German law specifies that the royalties are to go to the author of the work. Claims are made through the collecting societies and each copyright owner is "entitled to an equitable participation." §54(b) (1985 Amendment). The Austrian law also specifies that the compensation is to go to authors, performers, and producers of phonograms and that claims are only to be made by collecting societies. In Hungary the fee goes to the Bureau for the Protection of Authors' Rights; 50% of the fee goes to authors, 30% to performers, and 20% to the producers of phonograms. The law of the Congo says that compensation is due to the author and is payable to the professional body of authors. Finland envisions the fee as direct compensation to the holders of copyright and as indirect compensation for the joint purposes of the authors, i.e. the promotion of the arts. The Finnish fee also goes to a collecting society for distribution. The Iceland law says the authors of works are entitled to this remuneration and that it is to be collected and distributed by a joint collection center of a federation of copyright holders, including performing artists and producers.57/

c. Tax. Another method is to place a tax on the equipment/media; the revenue goes directly to the government but may be shared with copyright proprietors in some cases. Therefore, "any share that the beneficiaries might obtain from the tax revenue could not be seen as a compensation for the use

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57. See, App. III, for a comparison of the laws of the countries that now provide either a royalty or a tax on the blank tapes and/or the audio recording equipment.

made of their creations or contributions, but merely as a kind of support based on cultural policy considerations. Consequently, such a system has nothing to do with intellectual property rights."58/ Norway, Sweden, and Turkey have a tax. The Norwegian law places a tax on equipment and tapes; the Swedish law only on tapes. In both countries a part of the tax goes to copyright proprietors.59/ The Turkish law placed a tax on blank cassettes. The accumulated funds are to be shared annually between the "professional unions" to provide social amenities or services for their members. None of the money goes directly to copyright owners.60/

Thus, the major difference between the royalty and tax approaches is that the tax is probably outside the international copyright conventions; foreign copyright owners, therefore, need not be compensated even if domestic copyright owners are. Under royalty schemes, foreign authors and copyright owners are entitled to a share of the royalties under the principle of national treatment.

To the best of our knowledge American copyright proprietors have never collected any royalties from those countries that already require compensation for home taping. Gillian Davies observes that if the "remuneration is based on a specific right, this will involve payment to foreign beneficiaries," and she maintains that the legislation in both

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58. UNESCO/WIPO report, supra note 48, at 32.

59. Id. at 20.

60. Davies, EEC study, supra note 31, at 186.

Austria and the Federal Republic of Germany gives rise to national treatment under the international conventions and obligates these states to pay a share of the royalty to foreign beneficiaries.[61]

That some industrialized countries may nevertheless be prepared to demand reciprocity and refuse to accord national treatment protection is increasingly evident at international copyright meetings. The countries object to paying the bulk of royalties collected by them to American copyright owners--given the popularity of our works abroad--unless their authors are compensated for home recording in the United States. The demand for reciprocity may be enforced at the administrative level, *i.e.*, in the distribution decisions of the foreign collective society. Individual U.S. authors may not have legal standing to enforce their claims in foreign countries except through a U.S. collective society. No U.S. society will exist unless home recording royalties must be paid under U.S. law.

2. *Technical Measures*. Taping of copyrighted works could also be prevented through the use of technology by introducing scrambler or spoiler systems. This has already been done by pay television stations and is even now being attempted to keep satellite dishes from picking up pay signals.[62] At this point no truly satisfactory device[63]

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61. Davies, EEC study, *supra* note 31, at 161.

62. *See*, *Broadcasting*, September 23, 1985, at 30; *Cablevision*, September 30, 1985, at 14.

63. *See*, UNESCO/WIPO report, *supra* note 48, at 31.

exists that copyright owners can use unilaterally to inhibit audio taping.64/ Such a device might be feasible for audio works in the future, however, since engineers have refined the technology for an automatic jamming device that prevents the copying of motion pictures from prerecorded cassettes, cable, and broadcast signals. Copyright owners could be forced to resort to this technology if dual video recorders, already on the market in other countries, ever become a problem in this country.65/

Two main problems stand in the way of a technical solution. It generally provides a system that inhibits all copying of a copyrighted work, even when a copyright proprietor might wish to permit certain taping.66/ Also, technology not yet dreamed of will likely impede or vitiate the efficacy of any technical solution.

3. Judicial Resolutions. In a recent British case, Amstrad Consumer Electronics v. The British Phonographic Industry, Ltd., the plaintiffs, Amstrad, sold dual audio recorders with two decks on which it was possible to reproduce cassettes at twice the normal playback speed. In April of 1984

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64. Apparently, it is now possible to prevent audio taping if manufacturers place a chip in hardware to respond to a signal placed in the recording media by the copyright proprietor.

65. Dual recorders are already marketed here; they range in price from $200 to $460. See, Feldman, "Double Wall Decks Do More Than Just Dub," 1 Audio Retailer 10 (October 1985).

66. This could be resolved, however, if the copyright proprietor produced two different versions with a higher price to be paid for the version that permitted duplication.

the British Phonographic Industry (BPI) which represents most of the record companies in the United Kingdom, wrote to Amstrad expressing concern that advertisements for these machines encouraged members of the public to break the copyright law. At the end of 1984 BPI's attorneys sent a letter to Amstrad alleging that Amstrad's marketing of the dual tape decks "was calculated within the meaning of section 1 of the Copyright Act of 1956 to authorize unlicensed reproduction of their members copyrighted works." In the present action[67] Amstrad sought a declaration that they were not acting unlawfully in marketing their audio systems. The High Court found that Amstrad was encouraging purchasers to buy the units for the high-speed, double-tape facility, that they must know the units would inevitably be used to infringe, and that some units had been used to infringe. The High Court also found that it was irrelevant that Amstrad sold to retailers and not to the public and found that Amstrad approved and gave countenance to infringement. The court refused to grant declaratory relief and cited cases where courts were prepared to intervene in cases of aiding and abetting infringement of industrial property rights, by the supply of non-infringing equipment.

The appeal in this case of first impression was due to be heard in late September. BPI is now suing to have all dual cassette recorders removed from the market.[68]

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[67] In a different action which has not been resolved the copyright proprietor is suing Amstrad. 8 EIPR 138 (1985).

[68] Id.

The question of whether audio home taping is an infringement of copyright has not been presented to an American court.69/ Professor Nimmer argues that there is no exemption from copyright liability for audio home taping in the Copyright Act.70/ The recording rights coalition group would deny this. In the Betamax 71/ case the Supreme Court examined home video taping for private use. The Court explicitly approved the district court's finding that time-shifting for private home use must be characterized as a noncommercial, nonprofit activity. In concluding that such time-shifting was a fair use, the Court emphasized that since the television audience had been invited to watch the entire program earlier, reproduction of the entire work does not have its "ordinary effect of militating against a finding of fair use."72/ The opinion does not directly address off-air taping of cable transmissions and subscription television, nor the case of taping for purposes of "librarying."73/

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69. The German courts fully litigated the question of whether private taping was an infringement of copyright and concluded that it was before 1965 when a royalty was placed on recorders. See the discussion in the Seemann article, supra note 51.

70. See, Nimmer, "Copyright Liability for Audio Home Recording: Dispelling the Betamax Myth," 68 Va. L. Rev 1505 (1982).

71. Sony Corporation of America v. Universal City Studios, Inc., 464 U.S. 417 (1984), rev'g, Universal City Studios, Inc. v. Sony Corporation of America, 659 F.2d 963 (9th Cir. 1981), rev'g, 480 F.Supp. 429 (C.D. Cal. 1979).

72. Id. at 450.

73. The only reference to librarying is found at note 39, p. 453.

It could be argued that our Supreme Court would respond differently to a case involving audio home taping since both librarying and the use of dual audio recorders would be at issue; however, this seems unlikely. In fact, the Supreme Court has already indicated that it is up to Congress to make any change in the Copyright Act necessary to encompass taping of copyrighted works.[74] This sentiment is reflected in earlier statements made by the Copyright Office observing that Congress is the law giver and that a legislative change, if warranted, is the most appropriate way to shape a solution that will "bind all parties concerned."[75]

III. SOME CONCLUDING REMARKS

The Congress has considered various home recording bills for several years now, and has heard arguments for and against compensation for private copying in several hearings. The parties have commissioned, published, or cited numerous statistical studies that show that record sales decline as audio recorder penetration of the market increases and as sales of blank tape increase (proponents), or that home tapers purchase most of the records sold and that perhaps one-half of the taping is noninfringing (opponents). The Congress, as is often the case, faces a difficult task of assessing and balancing the equities. At the conclusion of this balancing analysis, Congress may reject any compensation for home recording for the time being because the need for the legislation has not been established through sufficient evidence of adverse impact on copyright owners and creators to offset the cost of the legislation for consumers. Alternatively, Congress may decide that we have had enough experience in this country and abroad to conclude that copyright owners and creators are harmed to some degree by the high incidence of home taping and they should be compensated; the legitimate interests of consumer groups can be accommodated by a reasonable, set royalty rate and by generous exceptions for noninfringing uses in computing royalties.

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[74] 464 U.S. 417, at 456.

[75] Video and Audio Home Taping: Hearing on S. 31 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. 51 (1983) (statement of David Ladd, Register of Copyrights); Copyright Infringements (Audio and Video Recorders: Hearings on S. 1758 Before the Senate Committee on the Judiciary, 97th Cong., 1st and 2nd Sess. 361, 363 (1981-1982) (statement of David Ladd, Register of Copyrights).

Ultimately even the consumer could benefit from such a system since arguably the royalty to the copyright proprietor will result in a greater range of musical selections, and a compensation system would obviate any need for copyright proprietors to resort to technology to inhibit taping activities.76/

If compensation for home audio recording is deemed appropriate, a legislative solution is clearly preferable.

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76. Some copyright owners now use signal scrambling technology to inhibit the unauthorized reception of copyrighted programming by back-yard satellite dishes.

A. Why a Legislative Solution?

The German experience in dealing with the home taping issue is especially enlightening. Although the German Supreme Court fully considered this issue and held there was copyright liability on the part of manufacturers and retailers of home taping equipment, it was the German Parliament, the legislative branch, that ultimately worked out a specific statutory compensation scheme which permitted uninterrupted home taping upon the payment of a royalty to the copyright proprietor. The Betamax decision illustrates that the legislative branch is also the appropriate body to resolve this issue in the United States. International studies also emphasize that a legislative solution is necessary.

Legislative solutions that provide for a royalty or levy that goes directly to a copyright collecting society for distribution to copyright proprietors seem to balance the equities involved more appropriately--by providing payment that goes to copyright proprietors and at the same time permitting unrestricted access to copyrighted works for private or home taping.

B. Why a Compulsory License With a Set Rate?

Both Germany and France77/ have tried schemes that called for voluntary reporting. In Germany only about 5,000 of millions of owners signed up voluntarily for the annual

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77. The French tried a voluntary system to impose a tax on recorders. See, Variety, Sept. 7, 1983, at 37.

license.78/ The German experience with the 1965 provision also reveals why a set fee is better than a negotiated one. The negotiations were protracted, the expected fee was never reached, and payments to copyright proprietors were delayed.

S. 1739 sets a fixed royalty rate and provides for adjustment of the royalty fees every fifth year. In adjusting the fee, the Copyright Royalty Tribunal will be guided by criteria that attempt to balance the equities.

C. Why a Royalty on Blank Tapes?

Again the German experience is helpful, and it suggests that a royalty on both recorders and tapes is best. The audio recorder market in the United States is similar to the German one: the German market is stagnant; the American market may become so since almost every American household already has at least one audio recorder.79/ This is reflected in the decline in sales of audio recorders for 1982 and 1983.

Also it seems appropriate to pay royalty on the tape itself. Sales of blank audio tapes continue to escalate, and most of the studies indicate that the majority of audio taping is of copyrighted music. Moreover, S. 1739 provides for exemp-

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78. Seemann, supra note 51, at 238.

79. Since many of the cheaper audio recorders do not have a long life span, the American market for audio recorders may continue to be a strong one.

tions for certain uses including those that are noninfringing--use in schools and libraries, for example--and for devices or media unsuitable for high-quality recording of copyrighted music.

D. Why Distribution by the Copyright Royalty Tribunal?

All of the countries that have placed a royalty on audio recorders or blank tapes provide for distribution through national collecting societies for authors' rights that were already in existence or were formed, as was the German ZPU, to receive these particular copyright claims. It has been suggested that the compensation for the prejudice caused copyright proprietors by home taping should be collected "globally and as far as possible by a single body, public, private or mixed, which would be responsible for distributing the proceeds among the different categories."[80] Realization of such a system is certainly not in the immediate future. Although arguments have been made that private collecting societies should handle this kind of distribution, it seems most efficient and practical at this point to rely on the Copyright Royalty Tribunal which is already in place rather than organize a new central organization such as the German ZPU.

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[80] UNESCO/WIPO report, *supra* note 48, at 15.

E. Does the Royalty Go to the Intended Beneficiary?

As noted earlier those countries with a royalty have tried to compensate the appropriate copyright proprietors. Realizing the difficulties inherent in a system that required each beneficiary to put forward an individual claim, they have instead opted for claims to be made through collecting societies.[81] While such a solution may not be perfect, copyright owners themselves clearly prefer collective society distribution systems to a system that provides no compensation for unauthorized copying of copyrighted works.

One way to meet the ARRC criticism that the royalty does not go to the intended beneficiaries would be to set out a general distribution scheme that calls for a certain division in the act itself. The Hungarian law requires that the royalty on blank audio tapes is distributed as follows: 50% to authors, 30% to performers, and 20% to producers. The French law also specifies a distribution rate.[82]

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81. UNESCO/WIPO report, *supra* note 51, at 33.

82. *See*, App. III.

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Mr. Chairman, S. 1739 is a distinct improvement over bills considered in previous congresses. Further fine tuning will naturally occur, but the overall approach of the bill is sound, assuming you conclude that copyright owners should receive some compensation for home audio recording of their works.

As you well know, copyright legislation is enacted under the rubric of the Constitution's Copyright Clause. The oft-stated purpose of that Clause is to benefit all of society by stimulating the creative impulse in relatively few people through a grant of property rights known as the copyright law. This bill, like all other copyright measures, should be tested against the constitutional purpose: is compensation to copyright owners for home audio recording likely to invigorate creative instincts, and encourage the creation and wide dissemination of the works thus created? In the long-term, will public benefit from the availability of new creative works outstrip the added cost to the consumer of audio recording devices and media? That is a judgment for the Congress to make on behalf of the public as a whole.

Thank you. I will be pleased to respond to any questions.

HOME TAPING STUDIES, REPORTS, OR SURVEYS

APPENDIX I

International:

Davies, Gillian, Private Copying of Sound and Audio Visual Recordings (1983) [EEC Study].

IFPI, Private Copying of Sound and Audio Visual Recordings (Survey of non-EEC Member States of the Council of Europe (1983) [Council of Europe Study].

Secretariats of Unesco and WIPO, Unauthorized Reproduction for Private Purposes of Sound and Audiovisual Recordings, Broadcasts and the Printed Word (June 1984).

United States:

A Study on Tape Recording Practices among the General Public, conducted for the National Music Publishers Association (NMPA) and the Recording Industry Association of America (RIAA) by the Roper Organization Inc. (June 1979).

A Survey of Households with Tape Playback Equipment, commissioned by the Copyright Royalty Tribunal and carried out by R. Hamilton & Staff (September 1979).

Blank Tape Buyers - Their Attitudes and Impact on Prerecorded Music Sales, prepared by CBS Records Market Research (1980).

A Consumer Survey - Home Taping, prepared by Warner Communications Inc. (1982).

Audits & Surveys: Home Taping in America 1983: Extent and Impact, prepared for the RIAA (1983)

Yankelvich, Skelly and White, Inc., Why Americans Tape: A Survey of Home Audio Taping in the United States, prepared for the Audio Recording Rights Coalition (1982).

Audio Surveys in Other Countries:

The following list appears as Appendix I in the IFPI study on Private Copying.

APPENDIX 1

LIST OF AUDIO SURVEYS REFERRED TO IN THE TABLES

AUDIO SURVEYS

AUSTRIA	A1	Bericht des Österreichischen Gallup Instituts von September 1974 über die Ergebnisse einer im Auftrag der Firma AUSTRO MECHANA durchgeführten Untersuchung.
BELGIUM	B1	"Etude du Marché des Enregistrements sur Bandes et Cassettes". 1977. Survey commissioned by SIBESA (Syndicat de l'Industrie Belge d'Enregistrements Sonores et Audio-Visuels) and SABAM (Société Belge des Auteurs, Compositeurs et Editeurs).
DENMARK	S1	"Cassette Recording 1977 in Finland, Sweden, Norway and Denmark". Survey carried out in 1977 by the Nordic Omnibus.
	S2	"Gallup Survey concerning the Music Recording Habits in Finland, Sweden, Norway and Denmark". Survey carried out in January 1980 by Gallup Poll for Teosto, Finnish Group of IFPI, Nordisk Copyright Bureau, Swedish Group of IFPI, Norwegian Group of IFPI and Danish Group of IFPI.
FRANCE	F1	"Les enregistrements sur bandes et cassettes". Survey carried out by SOFRES for SACEM/SDRM/SNEPA. April 1976.
	F2	"Le monde de la musique: les enregistrements de disques sur cassettes". Survey carried out by Louis Harris - France Organisation. May 1980.
	F3	"Attitudes et comportements des Français à l'égard de l'enregistrement privé". Survey carried out by SOFRES and CETREC and commissioned by GIEL, SCART and SIERES. October 1981.
	F4	"Les enregistrements à usage privé". Survey carried out by SOFRES, May 1983.
GERMANY	G1	"Musik-Überspielung auf Leer-Cassetten". Survey carried out by GFM (Gesellschaft für Marktforschung mbH) for GVL (Gesellschaft zur Verwertung von Leistungsschutzrechten mbH) and the German Group of IFPI. April 1979.
	G2	Idem - November 1980.
GREECE	GR1	Survey on Audio Private Copying, IFPI Greek Group, 1979.
IRELAND	IR1	Survey of Recording Practices in Ireland. Survey conducted by the Irish National Group of IFPI, 1982.

NETHERLANDS	N1	"Onderzoek naar het maken van geluidscopieen op banden en cassettes door particulieren". Survey carried out by the Stichting voor Economishe Onderzoek der Universiteit van Amsterdam (SEO) for STEMRA (Stichting Tot Exploitatie Van Mechanische Reproductie Rechten der Auteurs) and NVPI (Nederlandse Vereniging van Producenten en Importeurs van Beeld- en Geluidsdragers). June 1976.
	N2	Id - September 1980 (field work done in 1979).
NORWAY	S1	see under Denmark
SPAIN	PS1	Survey carried out by Gallup, Estudios Comerciales y Sociológicos. Grabaciones Privadas de Obras Musicales. On behalf of : Asociación Fonográfica Española y Sociedad General de Autores, 16 July 1982.
SWEDEN	S1	see under Denmark
SWITZERLAND	SW1	"Enregistrement sur cassettes vierges". Survey carried out by the Société suisse de recherches sociales pratiques de Zürich à la demande du groupe national suisse de l'IFPI et de la SUISA, Société suisse pour la défense des droits d'auteurs en matière d'enregistrements de musique et d'émissions.
UNITED KINGDOM	UK1	"Tape Recording - Report on a Quantitative Survey". Survey prepared by the British Market Research Bureau Limited on behalf of the BPI (British Phonographic Industry) and MCPS (Mechanical Copyright Protection Society). November 1977.
	UK2	Id - January 1980 (field work: 4th Quarter 1979).
	UK3	Id - February 1982 (field work: 4th Quarter 1981)
UNITED STATES OF AMERICA	US1	"A Study on Tape Recording Practices among the General Public" conducted for the National Music Publishers Association (NMPA) and the Recording Industry Association of America (RIAA) by the Roper Organisation Inc. June 1979.
	US2	"A Survey of Households with Tape Playback Equipment" commissioned by the Copyright Royalty Tribunal and carried out by R. Hamilton & Staff. September 1979.
	US3	"Blank Tape Buyers - Their Attitudes and Impact on Pre-recorded Music Sales". Survey prepared by CBS Records Market Research. 1980.
	US4	"A Consumer Survey - Home Taping". Survey prepared by Warner Communications Inc. 1982 (field work done in 1980).

CONGRESSIONAL MATERIALS

APPENDIX II

Bills

H.R. 4783 - A bill to amend title 17 of the United States Code to exempt the home recording of copyrighted works on home video recorders from copyright infringement. (Introduced by Mr. Duncan on October 20, 1981).

H.R. 4794 - A bill to amend the copyright law to provide that the use of home video recorders are not infringements on the exclusive rights of copyright owners. (Introduced by Mr. Parris on October 20, 1981).

S. 1758 - A bill to amend title 17 of the United States Code to exempt the private noncommercial recording of copyrighted works on video recorders from copyright infringement. (Introduced by Mr. DeConcini on October 21, 1981).

H.R. 4808 - A bill to amend title 17 of the United States Code to exempt the private noncommercial recording of copyrighted works on video recorders from copyright infringement. (Introduced by Mr. Parris on October 21, 1981).

H.R. 5250 - A bill to amend the copyright law to exempt private, nonprofit recording of copyrighted works on video recorders from copyright infringement. (Introduced by Mr. Foley on December 16, 1981).

H.R. 5488 - A bill to amend title 17 of the United States Code with respect to home video recording and video recording devices and media for other purposes. (Introduced by Mr. Edwards on February 9, 1982).

H.R. 5705 - A bill to amend title 17 of the United States Code with respect to home audio and video recording and audio and video recording devices and media, and for other purposes. (Introduced by Mr. Edwards on March 3, 1982).

H.R. 175 - A bill to amend title 17 of the United States Code to exempt the private noncommercial recording of copyrighted works on video recorders from copyright infringement. (Introduced by Mr. Foley on January 2, 1983).

S. 31 - A bill to amend title 17 of the United States Code with respect to home recording and video and audio recording devices and media, and for other purposes. (Introduced by Mr. Mathias on January 26, 1983).

S. 32 - A bill to amend title 17 of the United States Code with respect to rental, lease or lending of sound recordings. (Introduced by Mr. Mathias on January 26, 1983).

S. 33 - A bill to amend title 17 of the United States Code with respect to rental, lease or lending of motion pictures and other audiovisual works. (Introduced by Mr. Mathias on January 26, 1983).

S. 175 - A bill to amend title 17 of the United States Code to exempt the private noncommercial recording of copyrighted works on video recorders from copyright infringement. (Introduced by Mr. DeConcini on January 26, 1983).

H.R. 1027 - A bill to amend title 17 of the United States Code with respect to rental, lease or lending of sound recordings. (Introduced by Mr. Edwards on January 27, 1983).

H.R. 1029 - A bill to amend title 17 of the United States Code with respect to rental, lease or lending of motion pictures and other audiovisual works. (Introduced by Mr. Edwards on January 27, 1983).

H.R. 1030 - A bill to amend title 17 of the United States Code with respect to home recording and video and audio recording devices and media, and for other purposes. (Introduced by Mr. Edwards on January 27, 1983).

H.R. 5938 - A bill to amend title 17, United States Code, with respect to the rental, lease or lending of sound recordings. (Introduced by Mr. Edwards on June 27, 1984).

Hearings

Home Recording of Copyrighted Works: Hearings on H.R. 4783, H.R. 4794, H.R. 4808, H.R. 5250, H.R. 5488, and H.R. 5705 Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Committee on the Judiciary, 97th Cong., 2d Sess. Parts 1 and 2 (1982).

Copyright Infringements (Audio and Video Recorders). Hearings on S. 1758 Before the Senate Committee on the Judiciary, 97th Cong., 1st and Second Sessions (1981/1982).

Audio and Video Rental: Hearings on S. 32 and S. 33 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Committee on the Judiciary, 98th Cong., 1st and 2d Sess. (1983).

Video and Audio Home Taping: Hearings on S. 31 and S. 175 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Committee on the Judiciary, 98th Cong., 1st Sess. (1983).

Reports

S. Rept. No. 162, 98th Cong., 1st Sess. (1983).

H. Rept. No. 987, 98th Cong., 1st Sess. (1983).

COMPARISON OF LEGISLATION IN COUNTRIES PROVIDING A ROYALTY OR TAX ON BLANK TAPES OR EQUIPMENT

APPENDIX III

Country	Date	Form	Compensatory Rate	Paid By	Administered By	Intended Beneficiaries	Exemptions Provided
Austria	July 2, 1980 (Am. January 1, 1982)	Royalty on medium (blank tapes)	2.25 Austrian schillings/hour	First distributor in Austria of suitable recording material	Collecting societies	Authors, performers, and producers of phonograms	Copies not for personal use
The Congo	July 7, 1982	Royalty on blank mediums	Percentage of selling price		Professional body of authors	Author	--
Federal Republic of Germany	Sept. 9, 1965 (Am. June 24, 1985)	Royalty on equipment and media	Sound recording device DM 2.50 blank tapes DM 0.12/hour	Manufacturer (Importer)	ZPU	Author - copyright owner	Equipment or tapes likely not to be used for private copying
Finland	June 15, 1984	Royalty on blank tape	(For 1984 only) 0.025 FIM/every beginning minute	Manufacturer or importer	(In 1985) Teosto the Finnish Composers International Copyright Bureau	Holders of copyright (direct compensation); promotion of the arts (indirect compensation)	On exported tapes, tapes used professionally, or to make recordings for the blind or deaf, and where excused by the Ministry of Education for "a special reason."
France	July 3, 1985	Royalty on blank tape	Proposed equivalent of two francs (21 cents)/hour on audiotape	Manufacturer or importer	Commission to be formed--representatives of State and rights organizations	25% each to authors, composers, performers, and producers	--
Hungary	November 20, 1982	Royalty on blank medium	8% of sales returns	Manufacturer or distributor	Bureau for the Protection of Authors' Rights (performers' share transferred to the Federation of Art Workers' Union)	50% to authors 30% to performers 20% to producers (on phonograms)	On tapes that are exported or not suitable for private use (studio equipment, dictating machines)
Iceland	May 30, 1984	Royalty on blank tapes and equipment	Equipment: 4% of import or manufacturing price. Audiotapes Kr. 10,00	Manufacturer or importer	Joint Collection Center of Federation of Copyright Holders	Authors, performing artists, and producers. Statute to set out amount to each	
Norway	June 2, 1981	Tax on machines and tapes	Machinery: 17.5% of highest price payable. Tapes 3 Norwegian crowns on audio tapes	Importers and Retailers	Government Treasury	Norwegian Government plus certain amount is to be shared with authors, performers, producers and a fund for special projects	
Sweden	June 24, 1982	Tax on blank tapes	Audio tapes 2 ore /minute of playing time	Manufacturer Registered Importer (or others under §9)	Swedish National Revenue Office	Swedish Government. Certain amount goes to authors, artists/musicians, and producers of phonograms	Allowances for exported tapes, tapes that have already been taxed, those taken back when sale is cancelled or those sold at a loss
Turkey	November 1, 1983	Tax on blank tapes	5% of price	Manufacturer Importer	Ministry of Culture and Tourism	Funds shared out annually to "professional unions" to provide social amenities or services for members	--

Responses to Questions Raised by Members of the Subcommittee Following the October 30, 1985 Hearing on S. 1739

1. Under the House version of this bill, you, as Register of Copyrights, would have to try to solve the problem of making the proposed exemptions really work. According to one of the exemptions, blank tape which "will not be used for making audio recordings by individuals for private use" will be exempt. If I buy a tape and record one of my speeches, that tape shouldn't be taxed, but the tax would already be on it when I buy it. How do I get my money back? How do I prove I didn't use the tape to tape prerecorded music? Who do I prove it to?

1. Exemption for blank audio tape that will not be used for making audio recordings by individuals for private use: During the course of hearings on the various bills that were forerunners of S. 1739, several suggestions were made that could be used to accomplish this objective. These included royalty-exempt bulk orders, quarterly or semi-annual rebates from the manufacturer, and guarantees of purchase rights to individuals who make non-infringing uses.

It now seems more efficient to devise a system where the royalty is not paid on tape for non-infringing uses at the point of sale. If a minimal royalty is already on a tape that would be exempt, a system which permits the consumer to get a rebate upon proof of non-infringing use may be more troublesome to the consumer in the expenditure of time and effort necessary to get this rebate than the royalty itself.

Institutional use of blank audio tape for non-infringing purposes would be no problem since the institution could purchase all such tape with a royalty-exempt number similar to a tax-exempt number and provide this tape to individuals within the institution. This system could include businesses where a great deal of dictating is done, e.g., corporations, law firms. Congress should be able to purchase such royalty-free tapes for resale in outlets such as the stationery stores to members for legitimate purposes such as recording a speech.

There may be more of a problem for an individual who wishes to buy a tape for non-infringing home use when this individual is not associated with a qualifying institution or organization. It might be possible to provide each purchaser of an audio recorder with one or two royalty-exempt blank tapes.

It has been suggested that there are several types of tape available on the market and that a quality suitable for speeches but not for the recording of music could be exempt from this royalty as tapes suitable only for dictation would be exempt. Certain members of the consumer's groups have said that they buy higher quality blank tape and audio recorders for both business use and to listen to music in their homes. It does not seem unreasonable to have a minimal royalty on tape that is capable of both infringing and non-infringing uses. Also under the institutional or business outlet system, such a consumer could probably buy these tapes for business purposes without paying any royalty.

Almost every country that has placed a royalty on blank tape provides an exemption for tapes that are not suitable for private use or not likely to be used for private copying. It might be helpful to explore how these exemptions are handled in actual practice.

2. Is the CRT or the Register of Copyrights better able to figure out the answers to these questions?

2. Ultimately the best solutions will probably be those agreed upon by the interested parties. Either the Copyright Royalty Tribunal (CRT) or the Register of Copyrights would need additional staff to undertake this job. In theory the CRT may

be the better choice since the CRT is already doing this kind of balancing in other areas. Also former Registers, Barbara Ringer and David Ladd, have resisted rate-making by the Copyright Office on the ground that it would immerse the office in controversy. Although establishing exemptions from a congressionally mandated royalty should be less controversial than rate-making, there does not appear to be any reason to give this task to the Copyright Office if the CRT is given the task, as it is in the House Bill, of adjusting the royalty.

I a- Please comment on the responses given by the last panel at the hearing to my question about the lessons from the experience of other countries that have passed audio home taping royalty laws. I would like to have your reactions to two comments in particular. (1) Mr. Battaglia is of the opinion that all the countries that have adopted such a law have had difficulties with it, and if asked today would say they wish they hadn't ever legislated in this area. (2) Mr. Ferris, on the other hand, said he recognized that other countries had moved deliberately to implement a system such as S. 1739 proposes. He suggested, however, that the balance between the artistic producers and consumers is different in each country. It may be that the artists have comparatively less leverage in our country over copyright policy, but that isn't necessarily to our disadvantage: on the contrary, the evidence suggests that the balance we have struck has led to the most fertile creative environment in the world.

I a-(1) Mr. Battaglia's assertion seems unfounded for two reasons:

1. Five of the seven countries that have passed legislation placing a royalty on blank tapes have done so since July of 1982 and three of these five in 1984 or later. Their experience with the royalty has not, therefore, been long enough to make this kind of judgment.

2. The two countries that have had a royalty for the longest time--Germany on recorders only since 1965 and Austria on tape since 1980--have both amended their laws but have done so in order to increase or strengthen the rights of the copyright proprietors. Austria increased the royalty on blank tapes in 1982; Germany amended its law on June 24, 1985, to

> require a royalty on tapes as well as equipment, to set a specific instead of negotiated rate, and to permit authors to demand sales figures from manufacturers and importers so that levy revenues can be determined.

Germany has had the most experience with this legislation and these recent amendments make it easier and more worthwhile for the copyright proprietor to benefit from this compensation.

It can be said, however, that countries who have recently passed legislation or are now considering such legislation have benefitted from the German experience and the United States should also; see, the response to question II d *infra*.

(2) Mr. Ferris's remark is three-pronged: (i) the balance between artistic producers and consumers is different in every country; (ii) artists in our country may have less leverage over copyright policy; and (iii) this is not necessarily to our disadvantage since our balance has led to the most fertile creative environment in the world.

The first two prongs of this assertion are probably true, but the third does not necessarily follow in the sense that Mr. Ferris intended, *i.e.*, if we have the most fertile creative environment in the world (an unproven proposition), it is not necessarily due to giving artists less leverage in copyright policy than consumers. This is especially true if Mr. Ferris means that consumers should exploit works protected by copyright law for free or that absent compensation this creative environment will continue to flourish. Many authors, including Americans, in the past and present, have had an outside job in order to make a living either until they were successful or for all of their creative lives. There is no evidence, however, that this adversity caused their creativity to flourish. Artists who are forced to accept noncreative employment spend less time in creating. In fact periods in which art flourished such as the Elizabethan or Renaissance eras are usually ones in which rulers or governments provided effective compensation to creators (at that time, through patronage).

b- **What are your thoughts on this possible alternative to S. 1739 that has been suggested. The idea is to pass a law that requires that electronics manufacturers insert a decoder chip (a technology now available according to our information) in every machine that they make after a certain date. This would enable the copyright owners to market two types of records and prerecorded tapes, one copy-proof, and another capable of being copied. Thus they could recoup the loss of sales due to home taping by charging a higher price for the copiable version, and no added royalty on the recording machines would be necessary.**

b- On the surface this solution sounds good. It does, however, require cooperation on both sides. Reluctance on the part of manufacturers to insert a decoder chip would suggest that they are not completely sure of their argument that a great deal of home taping is non-infringing.

In practice there may be several other problems with the electronic solution. This solution would not keep owners of pre-decoder equipment from making uncompensated copies of copyrighted works. Also there would probably be even more of a rush than under S. 1739 to buy equipment before decoder chips were added. Since no royalty would be on individual tapes, consumers could band together to make multiple copies from one copiable prerecorded tape.

It might prove easy for someone with technical knowledge to remove the decoder chip from the equipment and thus permit the consumer to continue to make uncompensated copies of copyrighted works.

The price on audio recorders with decoder chips will have to include the cost of this inserted device. Ultimately this price will be passed on to the consumer. Some consumers in the future will argue that they do not record copyrighted music and should not have to pay for the decoder chip, but in order for this solution to be effective to any extent, every audio recorder capable of private use would have to contain a decoder chip. Thus, although the price may be less for decoder equipped recorders than the proposed royalty, this solution may not be a better way to eliminate payments on non-infringing recorders.

c- **How would this approach compare to S. 1739 in terms of our basic goals of insuring adequate copyright protection and compensation to copyright owners affected by home taping, and at the same time imposing minimum burdens on non-copyright-related uses of recording equipment?**

c- Unlike S. 1739 the decoder chip or electronic approach places no burden on non-copyright-related uses of recording equipment. On the other hand as discussed above, it might be easier to avoid any payment to the copyright proprietor for copyright-related uses under the electronic approach than under S. 1739. Pre-decoder equipment would permit copying of any tape or record released in the past or future. Decoder chips if in place would limit copying to that permitted by the copyright proprietor but would not limit the number of copies made. A royalty on blank tape under S. 1739 would ensure that compensation is made for each copy.

It is, therefore, essential that Congress weigh all of these factors before passing legislation that opts for an electronic solution that may turn out to be no solution from the copyright proprietor's point of view.

d- **If the decoder approach were adopted, I presume it would still be necessary to pass some sort of copyright exemption for non-commercial home taping, for even if the two types of records were marketed, the status of the activity of home taping would still be unsettled under current**

law. How would an exemption fashioned in conjunction with the decoder solution differ from that contained in the first section of S. 1739?

d- The proposed §119(a) standing alone could exempt home taping under an electronic solution. If, however, Congress wants to emphasize that prospective home taping of copyrighted material is legitimized only in situations where the consumer is taping the higher priced prerecorded cassettes, specific language will have to be fashioned.

As discussed above it would seem difficult to enforce such a restriction. In addition to the problem regarding already existing recorders, there is the number of copies permitted to be made per higher priced prerecorded copyrighted record or tape. It may be harder to tie the home taping exemption to the electronic or decoder chip approach than to a compulsory license.

II a- As you know, the 99th Congress is currently considering whether to join the Berne Copyright Convention. If we were to enact legislation like S. 1739, would it create any conflicts with the Berne Convention?

II a- S. 1739 does not now appear to create any conflicts with the Berne Convention. All of the countries that have passed similar legislation belong to the Berne Convention for the Protection of Literary and Artistic Works. Private copying or home taping of both audio and video works has been discussed at the intergovernmental level since 1977 when UNESCO and WIPO convened a working group to consider various exceptions to protection permitted by the International Conventions, Berne and the Universal Copyright Convention. This working group concluded that

(1) under Article 9(2) of the Berne Convention private use was not automatically lawful

(2) such reproductions were subject to the exclusive right of reproduction under the Berne Convention and that

> (3) as long as the state of technical progress did not allow copyright owners effectively to exercise the prerogatives of the exclusive right in the event of the private reproduction of videograms, the only solution seemed to be the establishment of a global compensation for authors or their successors in title ... in the nature of an indemnification for being deprived of the opportunity to exercise exclusive rights.[1]

Since 1977 international copyright groups such as UNESCO and WIPO have continued to study the ensuing copyright problems and look for solutions within the international conventions or national legislation.[2] It is clear that they will continue to do so since the general consensus is that copyright proprietors should be compensated for these uses.

b- Is there a possibility that our failure to enact audio home taping legislation could create problems for our joining the Berne Convention as it now stands or as it may evolve in the future?

b- It could create problems. The most recent international meeting held in June of 1984 under the auspices of UNESCO and WIPO on Unauthorized Private Copying concluded that private copying as engaged in today in many countries runs the risk of not being consistent with Article 9(2) of Berne. This group also recommended that countries consider measures to mitigate the adverse effects to copyright owners and authors of private reproduction of copyrighted works.

c- Do you agree that passage of the Act would strengthen the American position in arguing for enhanced protection for intellectual property in international fora. How might the manufacturers

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[1] See Davies, Private Copying of Sound and Audio-Visual Recordings 106-123 (1984).

[2] Report, Group of Experts on the Rental of Phonograms and Videograms, Copyright, 16 (Jan. 1985); Report, Group of Experts on Unauthorized Private Copying of Recordings, Broadcasts and Printed Matter, Copyright, 280 (July-Aug. 1984). See, EEC Study, Chapter 5, for a good summary of both intergovernmental Recommendations and International Non-governmental Recommendations.

of tape and equipment benefit from an improvement in America's ability to defend patents, copyrights and trademarks?

c- Yes.

If the United States does not compensate copyright owners for home taping, it cannot expect foreign countries to protect U.S. authors. Some countries now considering legislation that would provide compensation for home taping have already objected to paying the bulk of royalties collected by them to American copyright owners -- given the popularity of our works abroad -- unless their authors are compensated for home recording in the United States. The demand for reciprocity may be enforced at the administrative level, i.e., in the distribution decisions of the foreign collective society. Individual U.S. authors may not have legal standing to enforce their claims in foreign countries except through a U.S. collective society. No U.S. society will exist unless home recording royalties must be paid under U.S. law.

Manufacturers of both tape and equipment want the best patent and trademark protection available for their products. Since international protection is based on cooperation between states by unilateral treaty or international convention, it is in the interests of all American intellectual property rights holders to ensure that American protection of these rights is sufficient to permit America to argue for enhanced protection of intellectual property.

d- As we consider S. 1739, what can we learn from the legislation enacted in other countries? What particular pitfalls should the Congress be alert to?

d- Yes, we can learn a great deal from the experience in other countries. West Germany encountered several problems with the 1965 legislation:

1. The negotiated fee proved to be slow and cumbersome.
2. The ceiling on the negotiated fee was never reached, and copyright proprietors did not receive the amount of money that had been anticipated.
3. The levy was only on hardware, and the price of hardware dropped.
4. The hardware market stagnated, and sales slumped.

The 1985 German legislation placed the royalty on both hardware and tapes, set a fixed royalty rate, and gave authors the right to demand sales figures from manufacturers and importers.

We can also learn a great deal about distribution of royalties from other countries. If the funds collected are to go to the copyright proprietor, a royalty is best. In countries where there is a tax, little of the money collected may actually go to the copyright proprietor. Also if it is feared that the money may not go to the intended beneficiaries, a specific distribution scheme can be placed in the law as it has been in France and Hungary.

e- You noted in both your written and oral testimony that the definition of "audio recording" found in Section 119(d) is not sufficiently narrow to exclude certain video machines. As I mentioned at the hearing, I would appreciate it if you would provide the Subcommittee with a revised definition that we can incorporate into the bill at the mark-up stage.

e- The definition of "audio recording device" can be sufficiently narrowed by substituting the following language in section 119(d)(2): "which may be used primarily for making audio and not video recordings" for the language in lines 15-16 "which can be used for making audio recordings." Or you could add the language "and is not designed primarily for making video recordings," after "audio recordings" in line 16. A similar change may have to be made in 119(d)(3).

> f- **Critics of S. 1739 claim that it is an "anti-technology" bill. What are your thoughts on this charge? If royalties are imposed on the tapes and equipment used to make musical recordings in the home, will the Congress inadvertently stifle further development in these fields? If so, how will the legislation inhibit technological development? Will it direct the technology to less desirable pursuits?**

f- If the royalty is reasonable, it should not stifle either the advancement of technology or sales of equipment and tape. Although German sales of recorders slumped, this can be attributed to the fact that the market had become stagnant. It should be possible to find out what effect the 1965 law had on German technology. A loss of profits could possibly cut back on research, but it is expected that a royalty will be passed on to the consumer and the manufacturer or importer should not feel any substantial loss. While it is possible that a decoder chip solution might direct technology to less desirable or evasive pursuits, it is difficult to envision how S. 1739 would do so.

Representatives of the audio recorder and tape industries claim that uses of the equipment will continue to merge as technology develops and that S. 1739 will impede these advancements. They envision one audio machine capable of doing everything.

The most recent hearings on S. 1739 reveal that a division line is being drawn between creativity and technology. This should not be done. The AFL-CIO endorsed H.R. 5705

> not because we wish to take sides between industries but because it protects the legitimate interests of an industry which employs many of our most creative people and union members and which we hope will continue to employ them in growing numbers; because it

> correctly apportions the fruits of technological change so that all who are involved--composers, producers, manufacturers and retailers--have a share and lastly, because it provides a mechanism making it possible for the artist and technicians who make it all possible to realize some compensation for the enhanced use of their work.[3]

g- How does the unauthorized home taping of copyrighted material affect American workers? Have Americans lost jobs in the music industry due to home taping? How many American jobs depend on manufacturing or importing tape recorders or blank tapes and how would those jobs be affected by S. 1739?

g- The Copyright Office does not have the latest or best figures available on job loss or potential job loss for American workers in either the music industry or the audio recorder and tape industry. Various earlier statements indicate that the American recording industry has laid off a great deal of workers in the past few years. Reports also indicate massive unemployment and low wages among musicians. At the 1985 hearing a music industry economist said that jobs had fallen from the 1970's high of 29,000 to 19,000 by 1984. It is not possible to determine how much of this unemployment within the music industry is due to home taping.

Tape and recorder manufacturers and importers assert that jobs will be lost if a bill such as S. 1739 is passed. It is not clear how many American workers are employed in these industries. The 1985 U.S. Industrial Outlook reports that 95% of all video and audio recorders are imported. (pp. 476-7). In the Senate hearings on S. 1758 Joseph Lagore, a Sony representative testified that there were 6,000 workers for Sony

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3. Home Recording of Copyrighted Works: Hearings on H.R. 4783, H.R. 4794, H.R. 4808, H.R. 5205, H.R. 5488, and H.R. 5705, Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Committee on the Judiciary, 97th Cong., 2d Sess. 1075 (1982) (statement of Jack Golodner, Director of the Department of Professional Employees) (emphasis added).

in America and noted that "other countries are also involved in tape manufacturing, and if this industry were curtailed, the job losses could be significant." (p. 62). At the 1985 hearings on S. 1739 a Tandy representative testified that Tandy employed 27,000 American workers.

It should be possible to get accurate employment figures from the industries involved, but any loss claimed is speculative and seems designed to motivate Congress to act. The German tape manufacturer BASF threatened to leave Germany if legislation placing a royalty was passed. The German legislature responded by lowering the proposed royalty on blank tape.

Senator MATHIAS. Thank you very much, Mr. Oman.

The statement is often made that the current law is very clear on the subject. Can you shed some light on that proposition? Is this wholly true, or is it true in part?

Mr. OMAN. I think the best that can be said is that the law on the subject is unclear. In the *Betamax* case the legality of home audio recording was not the issue, and the question has not been adjudicated.

Senator MATHIAS. I would think you were a candidate for the Supreme Court. That is what the Supreme Court says to us, that the law is unclear, and that the Congress ought to clarify it.

Senator METZENBAUM. As I pointed out to Senator Mathias, everybody claims that the Supreme Court makes too much law. They claim the administration is trying to move into the prerogatives of the Congress. We welcome the Supreme Court, and we welcome you. We are very happy to have you take this responsibility, so you may have it. Be my guest.

Mr. OMAN. The legislative history of the Sound Recording Act of 1971, which addressed primarily the piracy question, contains what some people call loose talk on home taping. This language has not been held by the courts to have the weight of law in the 15 intervening years. The language in the House report was considered by the district court in the *Betamax* case. The court of appeals studied it and refused to apply it to the home video recording context. I think the best that can be said is that home audio recording is an unsettled area of the law. In the final analysis, consideration of the home taping issue was so scanty in the course of enacting the Sound Recording Act back in 1971 that it really would not do much good to dwell on a close examination of that legislative history. That history is a maze, and one that does not illuminate the problem that we are addressing today. We should probably not consider any of the statements in the past as binding, one way or the other.

We should consider the issue afresh, and I think that is the message that the Supreme Court was giving Congress in its decision in the *Betamax* case. Reduced to its essentials, the record shows that three Congressmen, and then Assistant Register of Copyrights Barbara Ringer, saw only that there was no reasonable means of enforcing a proprietor's right of home taping at that time.

If I may read a statement by Barbara Ringer, I think it helps us focus on the issues here today:

> My opinion, whether this is philosophical dogma or not is that sooner or later there is going to be a crunch here. But that is not what this legislation is addressed to, and I do not see the crunch coming in the immediate future.
>
> Other countries have felt it more directly than we, partly because record prices are lower here than in Germany. In that situation there is a range of legal devices for trying to keep the practice under reasonable control. But I do not see anybody going into anyone's home and preventing this sort of thing, or forcing legislation that would engineer a piece of equipment not to allow home taping.

So in conclusion, I would think that the issue is unsettled, and that we have no clear guidance from the courts as to whether home audio taping is illegal.

Senator MATHIAS. Ms. Schrader, do you want to add anything to that?

Ms. SCHRADER. The comment on home recording in the legislative history on the Sound Recording Act in 1971, as Mr. Oman has said, is thought by some to have been a passing remark, since the bill itself dealt with commercial piracy. You have the further question of whether Congress, in enacting the Copyright Act in 1976, which is the current copyright law, intended to retain any exemption that may have been part of the law before 1978. Finally, as Mr. Oman has said, the Supreme Court did not address the issue of audio home taping. The *Betamax* case concerned only video home taping.

Senator MATHIAS. Senator DeConcini.

Senator DECONCINI. Mr Chairman, I have to go to a conference committee on appropriations right at this moment. I wonder if the chairman would indulge me to ask just one question.

Senator MATHIAS. It is agreeable to me.

Senator DECONCINI. Thank you, and congratulations on your new appointment, Mr. Oman. We miss you here and we wish you well.

I am concerned that under the House version of the bill, and you touched on this in your statement, you, as Register of Copyrights, would have to try to solve the problem of making the control of the exemptions really work. According to one of the exemptions, blank tapes, which "will not be used for making audio recordings by individuals for private use will be exempt."

If I buy a tape to record one of my speeches, that tape could not be taxed, but the tax would already be on it when I bought it in the first place, as I understand it. How do I get my money back, and how do I prove that I did not use the tape for prerecording music? Maybe I used it for both; used it once for prerecording and erased it and used it again. Who do I prove it to and how do I resolve that? Do you have any suggestions for us?

Mr. OMAN. I think the thought behind it originally was that there would be different qualities of tapes: One quality of tape for home recording, which is the problem that we are addressing today, and one low quality that is used for dictaphones and recording speeches.

Senator **DeConcini**. I must say that is appropriate. [Laughter.]

So you would not have any tax on the low-quality political-speech tape. [Laughter.]

Mr. **Oman**. I am not sure that would be an official classification. [Laughter.]

Senator **DeConcini**. In any event, you would solve the problem by having two types of tape, is that right?

Mr. **Oman**. That is the idea.

Senator **Mathias**. Senator Metzenbaum.

Senator **Metzenbaum**. I am curious about these two types of tape. I am wondering if you can do that, whether we need any bill at all, and whether you do not almost zero in on the issue right at the outset. Let me back up a minute.

Is there any law now that says it is illegal literally to pirate somebody else's work?

Mr. **Oman**. Piracy, I think, is a technical definition, which means the commercial exploitation of somebody's copyrighted work; there are laws that do prohibit that type of activity.

In terms of preventing a homeowner from recording off the air, or recording from a phonograph or a disc player for private, noncommercial use, there are no laws on the books in this country that would prevent that type of activity.

Senator **Metzenbaum**. Well, is the state of the art in this particular field that there are these two categories about which you speak, or is it the fact that the person making a recording at home wants to use the highest quality recording in order to get the best quality music or political speech, as it may be, in their homes?

Mr. **Oman**. Well, certainly, if the purpose is to copy a recording for one's subsequent use, one would want to have the highest quality tape available, and that is the tape that would be covered by the House bill and by the Senate bill.

Senator **Metzenbaum**. So then, should the definition be amended to make certain that the royalties are only on tapes or recorders that are used primarily for audio recordings?

Mr. **Oman**. There has been some evidence introduced that suggests that new technology has enabled some of the video machines to be used for taping of audio programs, and some of those videotapes have recording durations of up to 24 hours. It is felt that this type of tape is not the type of tape that we were contemplating in the House bill or the Senate bill, and that this type of tape should be specifically exempted.

Senator **Metzenbaum**. I will be interested in hearing the other witnesses who are probably more expert in this field than you, and should be.

Mr. **Oman**. I have no doubt that their expertise——

Senator **Metzenbaum**. I did not mean that in a disparaging manner. That is their field.

I also want to welcome you in your new responsibilities and tell you that I am pleased to see you on that side of the table, which gives you more money, I assume, more prestige. [Laughter.]

At least I hope so.

Senator **Mathias**. And a better boss. [Laughter.]

I have just one further question. This bill does not specify a formula for distribution of the royalties. Senator Metzenbaum raised in his statement the question of who is going to benefit. Many others are also curious about whether the creators of new music or less prominent, less well-known artists will see any of the royalties, or are they all going to go to the superstars who are already rolling in money.

You pointed out that some countries have adopted home audio tape copying laws, and have taken an interesting tact. Some have specified as to whom the proceeds should be distributed.

There have been similar suggestions made here. There have been suggestions of a pension fund for artists, or perhaps contributions to the National Endowment of the Arts. Do you have any views for these alternative approaches?

Mr. OMAN. If there is a genuine fear that all the proceeds go to the "fat cat" record companies, I imagine that you could direct that certain percentages go to different categories of recipients. Some countries have a specific payback provision. In France, authors would get 25 percent, composers would get 25 percent, performers would get 25 percent, and the record producers would get 25 percent. Hungary gives 50 percent to the authors, 30 percent to the performers, and 20 percent to the producers.

In your bill, Senator Mathias, the Copyright Royalty Tribunal would make that judgment. It would sort out the equities, and make its judgment possibly a 50/50 split or a 60/40 split—depending upon how they saw the equities and how they saw the respective contributions that were made in creating the work. They perhaps would benefit from increased guidance from Congress and would welcome being left less to their discretion.

I would think that such an amendment could be easily drafted if you wanted to pursue that.

Senator MATHIAS. I will ask Ms. Schrader a question.

There have been suggestions that S. 1739 is inconsistent with the *Betamax* decision. Do you think that in fact the approach taken in this bill is consistent with the ruling of the Supreme Court in *Betamax?*

Ms. SCHRADER. In general, I would say the bill does not touch the ruling of the court in *Betamax,* because that ruling dealt with taping of video programs. The court also did not address the question of "librarying" of videotapes, so to the extent that Congress believes that the problem in the case of audio recording is "librarying," that is retention of the tapes, the court really has not addressed that issue. In any event, I think the court gave a clear signal that home recording in general is an issue for the Congress to resolve through legislation.

Senator METZENBAUM. There is one basic issue that has always bothered me about this legislation or anything similar to it. I think everybody would agree that it is wrong for X to steal the music, or whatever, from somebody who has produced it. I do not think it is wrong for the homeowner to make a copy, because I do not see that as being pernicious, but I do think there is some evil in somebody else making a copy and then reselling it.

What has always bothered me about this legislation is that it does not strike at the heart of the issue. All it does is say that we are going to put a tax on everything, whether it is copied or not, and I guess then by implication we are suggesting that we really look favorably on this practice, and you can do it to a fare-thee-well.

Now, how does that deal with the basic wrong of stealing the property of another individual or group of individuals?

Mr. OMAN. I think the larger question you are addressing in terms of the commercial exploitation is adequately covered in the anticounterfeiting laws and sound recording piracy laws that we have. The question we are addressing here is a narrower one than the one of commercial piracy. It is whether or not a homeowner, enjoying a public performance in his or her own home, on whatever media, can copy that performance and repeat it at leisure down the road.

Senator METZENBAUM. We take care of that in one section. That we are seeing explicitly, I think, in the first section, that there is nothing in this bill to stop that.

Mr. OMAN. As a matter of fact, it makes it lawful for the first time. I think that is really the positive aspect of the bill.

Senator METZENBAUM. Let us just pass that.

What about the rest of the bill?

Mr. OMAN. The rest of the bill is an attempt by the sponsor to balance that grant of a right which now does not exist explicitly with what is considered fairness to the creators and supportive of the creative process in this country.

I think an analogy can be drawn to the satellite "dish" area—one that we have not had to deal with yet in copyright—and we may never have to deal with, but in that case the copyright owners found evidence of the fact that people were buying dishes and enjoying their programming which was available off the air unscrambled. It was there for the taking. Copyright owners have started scrambling those signals, and people with dishes have to buy decoding devices that will allow them to pick up the transmissions.

Now, the question is whether satellite "dish" owners have a right to view the copyrighted owner's programming free of charge, and I think the answer is found in the reaction of the copyright owners. They say, no, you are going to have to pay for that privilege.

We have a similar situation in the audio home recording environment where the homeowner is now free to tape and reuse time and again the product of the creator. Whether he or she should be able to do that on a continuing basis without ever reimbursing the creator is the question before us, and there are obviously equities on both sides.

On one side there are the losses to the creators, the losses to the owners of record stores, and the losses in terms of the creative process. On the other side, such a proposal would hurt the home taper, it would hurt the manufacturers of the tape and the equipment, and conceivably it could hinder the development of new technology, which is an issue, I believe, that should be more closely examined.

Senator METZENBAUM. You bring in a new perspective on this bill that I have not heard suggested before. What I understand you have just said is that because we are spelling out the homeowners' rights, the homeowner or the person at home to make a copy, because of that first paragraph, then there follows that we ought to provide this compensation.

Now, frankly, I have not heard any hue and cry from individuals at home about the need to be protected, because I do not think anybody is really thinking about prosecuting individuals who make copies in their homes, and I have always felt, and I still believe, that the real thrust of this legislation is for the reason that I described, and that is because the industry says, well, these copies are being made, they are being pirated. We, therefore, ought to receive some compensation for that, and I find it to be a nonsequitur. I do not find that to be very realistic. I think what we ought to do is throw them in jail, do whatever else, for making copies without having the right to do so. That yellow light means be careful, do not go too far in what you are saying. [Laughter.]

But you have actually suggested a little bit to the contrary. You have suggested that the reason for this legislation is because of the first paragraph. I do not believe that those people making copies at home need any protection or need any new laws. I think nobody is going to prosecute them under the present laws as long as they do not do it for commercial purposes.

Mr. OMAN. Sure, but they do face some possible threats in terms of forcing the copyright holders to resort to technology, the way the satellite programming services are being forced to resort to scrambling technology. It would be in no one's interest, I think, to force the copyright owners to——

Senator METZENBAUM. If they had that technology available, they would have already used it, I am sure, just as they are using it in scrambling as it pertains to satellites. I think it is not that easy to create that technology.

Mr. OMAN. No, it is not. It is beyond our technology right now, but if there is no solution to the home tape problem, they may allocate money to developing that technology in the future.

Senator MATHIAS. In your written testimony you say the definition of an audio recording found in section 119(d) is not sufficiently narrow to exclude video machines.

Well, certainly it would be my intention in this legislation to exclude video machines. I would ask either of you, Mr. Oman or Ms. Schrader, to provide for us some language—a revised definition—that could be incorporated into the bill.

Mr. OMAN. We will be happy to do that, Senator.

Senator MATHIAS. Thank you very much.

Our next witnesses will appear as a panel. Mr. Stanley M. Gortikov, president, Recording Industry Association of America, of New York, NY; Dr. Alan Greenspan of Townsend & Greenspan, New York, NY; and Mr. George David Weiss, president, Songwriters Guild of America, New York, NY.

Gentlemen, in view of the number of witnesses who have to be heard this morning, I think it will be unfortunately necessary to establish a time limit.

I would suggest 15 minutes for the panel, if you want to take it, and you may divide the time as you like, if that is all right with Senator Metzenbaum. Your written statement will appear in the record as if read.

STATEMENT OF PANEL CONSISTING OF STANLEY M. GORTIKOV, PRESIDENT, RECORDING INDUSTRY ASSOCIATION OF AMERICA, NEW YORK, NY; DR. ALAN GREENSPAN, OF TOWNSEND & GREENSPAN, NEW YORK, NY; AND GEORGE DAVID WEISS, PRESIDENT, SONGWRITERS GUILD OF AMERICA, NEW YORK, NY.

Mr. GORTIKOV. Mr. Chairman, and members of the subcommittee, I am Stanley M. Gortikov, president of the Recording Industry Association of America.

We are allowed only a few minutes to convince you that the monumental problem of home taping is in fact a monumental problem—and that S. 1739 is a reasonable way to offset the harm. When I first appeared before you in 1982 to address the home taping problem, I showed you this picture of a then new machine recently introduced on to the market. This dual cassette recorder threatened to worsen the home taping problem by permitting tape-to-tape dubbing. Only 3 years have passed since that hearing, and already these dual cassette machines dominate the marketplace.

You have in front of you but a handful. At last count, we identified 254 different models from 56 different manufacturers. Some are big, some are compact. Here is one in my pocket that is so small that you can dub a tape while you jog. All of these machines have one thing in common; they exist primarily to copy prerecorded music, at two, four, even six times normal speed.

The story of the dual cassette machine is like the story of home taping. First it was an occasional hobby just for a few, and then it began to spread. Now it is a way of life for millions—the standard way to acquire prerecorded music without paying for it.

The problem has reached crisis proportions, and it affects not only the creators of music but all who listen to music. The amount of new music released in the marketplace has now declined for each and every year for 6 straight years.

In 1984 we released only about half the number of albums we released in 1978. Half! As Dr. Greenspan will describe, industry profits remained depressed, and opportunities for new artists and songwriters declined. How much longer can this go on? How much more visible must damage become? Are we to stand by passively and watch the greatest musical creative community in the world strangled by newer and newer generations of copyright killer machines? The worst is yet to come.

Here is Japan's newest weapon It is a triple deck machine with even greater capacity to rip us off. We ask for some relief from the tape and equipment manufacturers, because it is they who are benefiting at our expense. Their business and their products are virtually dependent on copyrighted music and recordings. Without that music, their products are merely mazes of plastic, wires, and chemicals. Only copyrighted prerecorded music gives them value, marketability, and profit.

Just look at how they merchandise their products in their own words. This one they call a "Tape Factory," and they say, "If one of your friends has a tape you want to own, copy it." That is clear intent.

Next, they call this a "Tape Collection Expander." That is clear enough as to intent.

The next they typify as a "Portable Cassette Factory," and the text says: "You have friends. Your friends have friends. Why not pool your resources and increase your cassette collection with the latest in high speed, high quality duplication." That leaves you no doubt.

The next one clearly says: "Save money. Copy a Friend's Cassettes."

And the last one says: "Beat the system. Copy your own cassettes."

So you need not rely on us to prove what are the dominant uses of blank tape and audio taping equipment. Rely instead on what the tapemakers themselves emphasize as to the uses of the product.

Here is a flyer from TDK, the major Japanese blank tape manufacturer, recommending unique applications of eight different tape formats to record almost everything our industry produces. Look at that list on the left side—every conceivable type of music: classical, jazz, disco, compact discs; you name it.

In short, the equipment makers and tapemakers sell their products by encouraging others to help themselves to our products. This displaces the sales which are the record companies' only source of revenue, sales which happen to be the lifeblood of the entire music community. This is obviously unfair and harmful to those whose careers and livelihoods are devoted to creating music, and it is also unfair to those who play by the rules and who pay for their music. One group of music consumers—those who tape—should not be able to shift the costs of creating and producing music entirely onto another group of music consumers—those who buy.

Ultimately, it is unfair to the entire listening public. Home tapers included, because it means less new music, less experimentation, less choice, less music to tape. Even the Nation's economy is hurt. American music is still one of the few American industries succeeding in world markets. Home taping blunts our competitive edge, reduces the amount of music that we can export to the rest of the world, and hurts our balance of trade.

So we urge you to respond to this situation by enacting S. 1739. Our efforts to respond to home taping in the marketplace have not made a dent in the problem. Our approaches to the Japanese manufacturers have been consistently rebuffed. As the Supreme Court said in the *Betamax* decision, the only alternative is a legislative solution.

We are not asking Congress to stop the taping. We are only asking that those who benefit from home taping pay something to those who are harmed by home taping.

[Following responses were subsequently submitted for the record:]

RESPONSES OF STANLEY M. GORTIKOV TO QUESTIONS SUBMITTED BY SENATORS METZENBAUM, MATHIAS, DECONCINI, AND LEAHY

Stanley M. Gortikov, President of the Recording Industry Association of America ("RIAA"), submits this response to questions concerning S. 1739, the Home Audio Recording Act. The first section responds to questions posed by Senator Metzenbaum at the hearing held on October 30, 1985, and the second section responds to questions submitted in writing by Senators Mathias, DeConcini and Leahy.

I. QUESTIONS RAISED AT THE HEARING

A. Record Company Profitability

At the hearing, Senator Metzenbaum questioned whether the record industry is now so profitable that this legislation is no longer necessary. In pursuing this inquiry, Senator Metzenbaum quoted references from a briefing paper submitted to this Subcommittee by the Audio Recording Rights Coalition (the "ARRC") which purport to demonstrate the recording industry's profitability.[1] The ARRC, which is the primary force behind opposition to this legislation, represents companies which manufacture and import blank tapes and taping equipment. Its contentions are both misleading and irrelevant to consideration of this legislation.

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[1] ARRC, "Taxing Blank Tape and Recorders: Untimely, Unnecessary and Unfair" (July 1985) (hereinafter "ARRC Pamphlet").

The fundamental principle underlying this legislation is that those who produce and create music have a right to be paid for the taking of their copyrighted property by those who tape rather than buy that music. The ARRC attempts to avoid the consequences of that principle by focusing instead on record industry profitability. But there is no means test in American property law. In short, making copyright protection dependent on proof of a sufficiently low profit level advances what the former Register of Copyrights referred to as a "sinister point-of-view: the idea that copyright is a mere privilege."[2]

Moreover, in harping on recording industry profitability, opponents of home taping legislation do more than just obscure the key policy question: they also base their case on data that are inaccurate, incomplete or inapposite. This is because they rely primarily upon recording industry revenues to establish the industry's profitability. Their analysis is thus flawed in several respects.

First, the revenues of 1984 -- which the ARRC claims to be the recording industry's best year ever -- were actually 33% below those of 1978 when measured in constant dollars. And indications are that 1985 revenues will not match those of 1984; in the first six months of this year, the recording industry reported unit sales 4.3% below those reported in the first half of 1984.

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[2] Remarks of David Ladd to ABA Section of Patent, Trademark and Copyright Law, Aug. 10, 1982.

More fundamentally, gross revenues prove nothing about recording industry profitability. As Dr. Alan Greenspan made clear in his testimony before this Subcommittee, profit margins for the recording industry as a whole have remained depressed even as revenues have improved. The statistics for 1984 -- the banner year, according to the ARRC -- bear witness to the accuracy of Dr. Greenspan's analysis. According to an analysis undertaken by Touche-Ross, the pre-tax income from the domestic sales operations of seven companies which together accounted for 80% of all U.S. record sales was only 3.7% of their revenues in 1984.

The Touche-Ross audit shows that in each of the last four years, a majority of the seven record companies which reported data lost money on their domestic record company operations. In 1981 and 1982, all these companies lost money. In 1983, while the industry recorded a small profit, six of the seven companies still lost money. And in the alleged banner year of 1984, when the industry's operating profit level was still 50% below the interest rate paid on passbook accounts, four of the seven reported losses on their domestic operations.

This consolidated income statement is attached to these responses, and we invite all interested parties to study it and then to compare it with the misleading anecdotal evidence on which opponents of home taping legislation have relied.

According to the ARRC, for instance, "WCI Record Group, including the Warner, Elektra/Asylum, and Atlantic labels, . . . called 1984 the 'biggest year ever.'" This quotation is taken completely out of context.

In fact, the article cited does not deal at all with Warner's domestic record operations, but rather deals exclusively with the performance in 1984 of the company's domestic and foreign music *publishing* operation.[3] This same publishing operation, along with Warner Communication's foreign record operations, accounted for the music and publishing division's increased operating income in 1983 as well -- a year in which there was a decline in the "domestic record labels' aggregate revenues and earnings."[4] And while 1984 was a strong year for the Warner Record labels, their success that year was attributable primarily to a few major hits. By definition, one cannot rely upon "exceptionally successful releases"[5] to provide income consistently from year to year.

The ARRC also finds it significant that "*[r]evenues* from MCA's Records & Music Group (which includes some domestic home video sales) jumped to $255 million in 1984 from the 1983 total of $188 million." (Emphasis added.) What the ARRC chooses to ignore is that even with this 36% increase in revenues, the operating margin of MCA's records and music segment -- including the contribution of home video sales -- was under 3.5%. And in 1983, when the recording industry as a whole registered a slight profit, MCA's recording operation lost almost $8 million.[6]

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[3] *Compare* *ARRC Pamphlet* at 4 *with* *Billboard*, Mar. 16, 1985 at 6.

[4] 1983 WCI Annual Report at 20.

[5] 1984 WCI Annual Report at 14.

[6] 1984 MCA Annual Report at 14.

Similarly, the ARRC quotes the 1983 RCA Annual Report as an indication that "sales of audio records and cassettes increased and, combined with strong controls, resulted in significantly improved profits." This language, of course, is wholly unilluminating -- it does not indicate how profitable the previous year was. Moreover, the ARRC cites the "record profits" of RCA's Consumer Electronics Division in 1984, apparently without realizing that the company's recording operations were no longer within that division. In fact, in 1984, earnings for the records and video subsegment of RCA Entertainment increased despite, rather than because of, sales of prerecorded music: "improved profitability of the joint ventures [to distribute home video software] more than offset higher artist investment and the start-up costs of a new audio-cassette manufacturing facility."[7]

With regard to the profitability of CBS, opponents of the bill do, at least, provide data concerning both profits and revenues in 1983 and 1984. But the sources the ARRC cites include not only the domestic recording operation -- CBS Records Division -- but also the CBS Records International Division, the Columbia House Division (record and tape clubs) and the CBS Songs Division (music publishing). And significantly, even if domestic record sales alone yielded the impressive profits noted for 1983 and 1984, they did so largely because the top spot of Billboard's album chart for much of the two-year period was held by one or another of three CBS releases: Michael Jackson's Thriller, Bruce Springsteen's Born in the U.S.A., and the soundtrack from Footloose.[8] Surely the ARRC cannot rest the merits of its position upon the mere fortuity of three successive blockbuster releases.

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[7] 1984 RCA Annual Report at 31.

As might be expected, the ARRC avoids entirely any discussion of less successful recording companies. For instance, it has never mentioned Thorn EMI, whose North American label, Capitol Records, sustained losses that put the company $5 million in the red during the financial half-year ending September 30, 1984.[9] Nor does the ARRC discuss Polygram Records -- which, according to a legal brief filed in 1984, sustained losses of $6 million in 1983 and expected to "finish 1984 about $15 million in the red."[10]

Thus, try as they may by picking and choosing among record companies for the very best data, opponents of home taping legislation cannot avoid the conclusions reported in a recent New York Times article:

> Profitable record companies are few and far between of late. The only record companies with nationwide distribution systems are Polygram, units of RCA, MCA and Britain's Thorn EMI and CBS and Warner. Of the list, only the last two are "really profitable."[11]

In sum, the ARRC is wrong when it focuses on recording industry profitability and wrong in its attempt to show that the industry is profitable. The ARRC is also wrong when it ignores the role of home taping in making the industry unprofitable. As a recent investment analyst's report noted:

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[8] 1983 CBS Annual Report at 23; 1984 CBS Annual Report at 25.

[9] Billboard, Jan. 26, 1985.

[10] New York Times, Nov. 3, 1985 at F16.

[11] New York Times, Nov. 3, 1985 at F16, quoting Mark Riely, entertainment analyst at F. Eberstadt & Company.

> In our opinion margins in [the recorded music] business will remain under pressure as unit growth is constrained by home taping and the demographic trend, and as price adjustments are hindered by the threat of increased taping.[12]

As that report went on to conclude, "[t]he proliferation of high-quality low-cost cassette tape recorders has created the industry's biggest problem."[13]

B. Antitrust Exemption

At the hearing, Senator Metzenbaum also asked about the reasons and precedents for the antitrust exemption contained in Section 119(b)(5) of the Act. The relevant language states:

> "Notwithstanding any provision of the antitrust laws, for purposes of this clause any claimants may agree to the proportionate division of compulsory licensing fees amongst them, may lump their claims together and then file them jointly or as a single claim or may designate a common agent to receive payment on their behalf."

Existing provisions of the copyright law support inclusion of this language in the Home Audio Recording Act. The antitrust exemption in the bill is virtually identical to those found in other provisions of the copyright statute that authorize the negotiation and/or distribution of royalty fees under existing compulsory licenses. For instance, virtually identical language authorizes joint activity by those owed royalties from the retransmission of copyrighted material by cable systems. See 17 U.S.C. § 111(d)(5)(A). Similarly, those claiming copyright royalties based on the use of their music in jukeboxes are permitted to act together so as to facilitate the distribution of those royalties. See 17 U.S.C. § 116(c)(2). And a third provision, which deals with the use of certain copyrighted materials by noncommercial broadcasters, contains a similar declaration: "[n]otwithstanding any provision of the antitrust laws" copyright owners may "negotiate and agree upon the terms and rates of royalty payments and the proportionate division of fees paid among various copyright owners and may designate common agents to negotiate, agree to . . . or receive payments." 17 U.S.C. § 118(b). See also 17 U.S.C. § 118(e)(1) (authorizing the negotiation of royalty rates between public broadcasting entities and owners of copyrights in non-dramatic literary works).

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[12] The Prerecorded Home Entertainment Industry, F. Eberstadt & Co., Dec. 14, 1983 at 1.

[13] Id. at 7.

None of these provisions gives rise to any potential for anticompetitive action. They all simply provide for the efficient functioning of the copyright system by making clear that "claimants may agree among themselves as to the division and distribution of [royalty] fees," S. Rep. No. 473, 94th Cong., 1st Sess. 82 (1975). See also id. at 103 (same).

In short, Congress has already determined that, with regard to other compulsory licenses, it is "economically beneficial" for claimants to coordinate their activities for the limited purpose of expediting royalty distributions. Broadcast Music, Inc. v. CBS, 441 U.S. 1, 16 (1979). Identical considerations mandate that the same beneficial practices -- undertaken for an equally limited purpose -- should be permitted under home taping legislation.

II. QUESTIONS SUBMITTED IN WRITING

A. Questions Submitted by Senator Mathias

1. An article in the October 20, 1985 New York Times said that spokesmen for the audio trade have pointed out that the royalties we are proposing would "add up to a handsome windfall for the record industry since the present royalties on recorded music usually run less than the suggested one cent per minute." If this is true, you would be better off collecting royalties from the sale of blank tapes than selling your own records.

a. Would you please explain how the copyright royalties on records are typically structured today?

b. How much would be generated by a one cent per minute royalty?

c. Please provide a representative breakdown for how you believe the royalty on blank tape will typically be distributed.

It is misleading and inaccurate to suggest that "present royalties on recorded music usually run less than the suggested one cent per minute." In fact, the royalties record companies pay to music publishers and composers alone amount to almost one cent per minute. Those payments, known as "mechanical royalties," serve as compensation for the use of musical compositions and are paid at a flat rate for each selection on each record sold. As of January 1, 1986, the statutorily set mechanical royalty rate will be increased from 4-1/2 cents per selection to 5 cents per selection, or .95 cents per minute of playing time, whichever is larger.

Mechanical royalties are shared by music publishers and songwriters, with songwriters customarily receiving about 50 percent of the royalties. These royalties do not, however, contribute at all to the compensation of the many artists, back-up musicians, vocalists, unions, and record companies whose efforts are essential to the creation of any sound recording. These participants in the musical recording process are compensated only by revenues from the sale of records -- millions of dollars of which are lost annually as a result of home taping.

Featured artists on musical recordings receive, by contractual negotiation, a percentage of the album's wholesale or suggested retail price. Typical artists' royalties today run anywhere from 22 percent to 36 percent of the wholesale price of albums, and the amounts may increase when a threshold level of record sales is reached.

Back-up musicians and vocalists are also compensated by sales revenues. First, they are paid a flat fee for performing in a recording session. In addition, record companies are obligated by contract to make contributions based on sales to union funds created to support musicians and disseminate their music to the public. Thus, about .35 of 1% of the list price of each record sold is contributed to the Music Performance Trust Fund, which collects $10-$18 million annually to hire union musicians to perform in free public concerts presented in 550 U.S. communities.

An additional .6 of 1% of the price of each record sold goes into the Special Payments Fund maintained by the American Federation of Musicians for direct distribution to those musicians who have performed in recording sessions at regular session rates. By union contract, AFTRA, the vocalists' union, also collects bonus payments for distribution to union performers when threshold levels of record sales are reached.

The record companies' contributions to composers, publishers, performers and unions -- not to mention any amount that they retain to support the creative infrastructure necessary for continued music production -- thus far exceed the modest one cent per minute royalty proposed in this bill. To suggest that S. 1739 provides a windfall to the recording industry is simply incorrect. In fact, Dr. Alan Greenspan has estimated that the Act will enable the music community to recoup only $200 million of the $600 million it loses annually as a result of home taping -- far short of full compensation to all the participants in the musical production process.

The compensation which is generated by the proposed home taping royalties will be distributed in the first instance to copyright owners whose musical works or sound recordings were played on the radio, broadcast on television, or sold in the form of records or prerecorded tapes during the year for which the royalties are collected. The copyright owners will in turn share royalties awarded them with others responsible for creating and producing the music on the basis of negotiated contractual agreements such as the ones discussed above. Royalties will thus flow from music publishers to composers and lyricists and from record companies to recording artists and musicians' and performers' unions. Because the terms of these contractual arrangements vary from company to company and artist to artist, it is not possible to specify the actual distribution of royalties across the industry.

2. One assumption that underlies this bill is that a great deal of the proceeds from these royalties will be used to help cultivate new musical talent and support some of the less profitable forms.

a. Can you explain how the industry currently allocates resources to that end?

b. What assurance can you give us that a portion of the proceeds from these royalties will be allocated to these worthy ends?

It is difficult to generalize about the means by which the music industry allocates resources to new and more specialized forms of music, since the allocation in any given year depends on the available talent, the available revenues, and the judgments of different individuals at many different record companies. It is nonetheless clear that record companies currently devote as much of their sales revenues as they can to the development of new music. Because virtually every recording released has a brief sales life, and because even star artists do not permanently retain their popularity, it is important for the very survival of the record companies that they continue to cultivate and promote new talent. Moreover, to the extent they can, record companies want to continue to provide the diversity of classical, jazz and other recordings the music community has been able to produce in the past.

Home taping siphons off the revenues that the music community has traditionally used to support these worthy goals. Enactment of S. 1739 will replace a portion of those revenues and will in some measure restore the ability of record companies to promote new talent and more specialized music. The assurance that a portion of the proceeds from the proposed royalties will be devoted to these ends is inherent in the very nature of the music business: it is in the interest of the music community itself to invest in new music to ensure that its products appeal -- and continue to appeal -- to a broad range of musical tastes.

3. When the Congress first addressed this issue back in 1981, the recording industry was doing poorly. Pac-Man and other video games as well as a stiff recession were eating into the record industry's market. In the past few years, the industry is doing exceptionally well and record sales are up dramatically.

a. How do you respond to those who say that this type of legislation is no longer necessary?

b. How do you respond to the charge that the industry's prosperity is to a large extent the result of the new technologies marketed by the audio equipment industry?

a. Those who say that this legislation is no longer necessary are saying that copyright owners are only entitled to compensation from those who use their property if their industry as a whole is losing money. This is a wholly disingenuous position for opponents of this legislation to take, since they argued that home taping legislation was unnecessary even when the industry was deep in its most unprofitable period.

Additionally, as discussed at greater length above, the profitability of the music industry is irrelevant to the need for this legislation: however significant it may be under some economic systems, a person's entitlement to compensation for the use of his copyrighted property is not, under our system of law, based on a means test. Finally, it is simply untrue that the industry "is doing exceptionally well." According to industry analysts, only two record companies have enjoyed consistently profitable domestic record operations. Even in 1984, when, according to the Act's opponents, the recording industry had its best year ever, four of the seven companies for which data are available sustained a loss on their domestic record operations. The relevant data are attached to this statement.

In short, the reason this legislation is still necessary is because home taping still displaces sales of prerecorded music; that displacement still deprives the creators and producers of the music of the compensation to which they are entitled; and the loss of compensation still serves as a disincentive to the creation and production of more music, especially that music whose profitability is most marginal, such as that by new artists or that which appeals to smaller audiences.

b. The music community does not deny that it benefits from the audio equipment industry: that industry has developed the hardware that can be used to play our music. Equally significantly, however, the audio electronics industry owes its success to the recording industry for producing software, without which its products would be much less valuable. To the extent that each group of products gives the other value, both industries profit from their use of the other's goods. In short, a symbiotic relationship exists between them.

Home taping, however, undermines this symbiosis because it enables the audio electronics industry to profit at the recording industry's expense. Manufacturers promote recorders as machines that enable consumers to get prerecorded music without paying anything to the copyright owners. In this regard, the relationship is not symbiotic, but parasitic, and requires a legislative solution.

4. According to Variety, retailers are complaining that failure to provide enough CDs may hurt overall sales because consumers are waiting for CDs rather than buying records. ("CD Consumers Want Unavailable Titles, But Won't Buy LP's," Variety, October 9, 1985, p. 117.) If, because of this failure to meet consumer demand, record sales fail to rise or even decline, is that an injury that should be compensated for by imposition of a royalty?

The recording industry is making every effort to meet the large, unexpected demand for CDs. If it does not do so and record sales fail to rise, or even decline, the record companies will forego sales revenue, at least until they can meet the demand.

We are not requesting compensation for any such losses. Our request for compensation is limited to reimbursement for the sales displaced by home taping -- a proven harm which is entirely unrelated to any gains or losses the industry may incur for other reasons.

5. S. 1739 provides an exemption to machinery containing technological innovations to prevent unauthorized home taping.

Please assess the status of the technological solutions that are being developed to "encode" the various tools used to copy audio materials.

Can we expect the marketplace to respond to the unauthorized home taping of copyrighted material? If so, please estimate how much the encoding mechanisms would add to the consumer's cost per machine.

Is it true that the manufacturers of recording equipment have refused to discuss with the recording industry the use of an encoding system that would provide a viable marketplace solution to the problem of unauthorized home audio taping? If not, please describe the status of these discussions.

At the hearing I invited anyone interested in this problem to recommend alternatives and amendments to S. 1739. Someone suggested legislation that would require all audio recording devices and all prerecorded phonorecords of every medium distributed after a given date -- for example, January 1, 1988 -- to contain the appropriate encoding mechanism. What is your reaction to that type of legislation?

Technology to prevent unauthorized taping of copyrighted material through encoding is available. It was developed by CBS Labs in 1982. The system operates as follows: In the recording studio, an inaudible signal is encoded in the master tape of a musical recording. A complementary integrated circuit, built into the next generation of recording equipment, acts as a sensor to detect the signal. When the inaudible signal is detected, the equipment's record mechanism turns itself off.

The circuit does not interfere with the recording of any noncoded material, whether from records, tapes or other sources. Thus, record companies would be able to market copy-compatible versions of their records by leaving them uncoded so as to permit taping. In addition, the present generation of equipment, and records and tapes, would not be affected.

After extensive testing, the coded signal has proved itself: it is impossible to hear, and it has resulted in no audible degradation in the quality of prerecorded music. Thus far, the circuitry has also proven highly reliable: it has accurately detected the encoding regardless of the quality of equipment on which the coded music is played and despite attempts to filter out the signal.

It is clear that the encoding mechanism is a low-cost marketplace solution to the problem of unauthorized home taping of copyrighted materials. The integrated circuit required to make the system work will cost just over $2.00. Moreover, the system is secure, since the integrated circuit cannot be removed from a recorder: such a removal would render inoperative the machine's recording capability.

Under the Home Audio Recording Act, any manufacturer that includes the necessary circuitry in its recording equipment will not have to pay any royalty on that equipment. Without the legislation, however, there is no incentive for equipment manufacturers to take steps to prevent unauthorized copying; in fact, their promotional campaigns are largely based on the advantages their machines offer for such copying. Legislation that encourages or requires the use of encoding equipment is thus a precondition to any marketplace solution.

The equipment manufacturers themselves have demonstrated the need for some legislative endorsement of encoding technology by resolutely refusing every recording industry approach to discuss it. Over the past three years, representatives of the international recording industry have sought meetings with the Japan Electronics Industry Association to no avail. Over a year ago, the Board of Directors of IFPI, the international recording industry association, even set one of its meetings in Tokyo in an effort to encourage representatives of Japanese equipment companies to meet to discuss various copyright concerns and matters of mutual interest. The meetings were requested directly with the companies, and were turned down. The meetings were requested through the Japanese Recording Industry Association, and were turned down. The meetings were requested through MITI, the Japanese government's trade industry division, and were turned down. Press and entreaties failed to engender a positive response. In short, the Japanese equipment industry refuses to talk, and instead balks at every effort to get it to respect the copyright interests of the American and international music industry.

This stonewalling by equipment manufacturers is especially galling when one considers that the head of the Japan Electronics Industry Association -- the group that refused to meet with us -- has lobbied this Subcommittee for protection of semi-conductor chips. Moreover, the Japanese government has never exhibited any hesitancy in approaching the United States government about protecting intellectual property in which it has a significant interest.

The RIAA would certainly favor a requirement that all audio recording devices contain encoding circuitry.

6. The Register of Copyrights testified that the definition of "audio recording" found in Section 119(d) is not sufficiently narrow to exclude certain video machines. Please provide a revised definition that will alleviate this problem.

The music community proposes the following language to remedy any ambiguities in the Act. Changes from current language are underscored.

> "(2) An 'audio recording device' is any machine or device, now known or later developed, which can be used for making audio recordings by individuals for private use, and which is capable of reproducing the sounds embodied in a radio or television transmission, or in a phonorecord or copy, by means of internal or external wire, cable or like connection between the equipment receiving or performing such sounds and the equipment reproducing them. The term 'audio recording devices' includes dual audio recording devices. Such term does not include a device (A) which is primarily used for reproducing motion pictures or other audiovisual works; (B) which is unable to receive the sounds embodied in a radio or television transmission, or in a phonorecord or copy, except by microphone; (C) which is capable only of performing such sounds (playback only equipment); or (D) which incorporates a decoder or similar mechanism that prevents the device from reproducing, or permits the device to reproduce, the sounds embodied in a phonorecord or copy in accordance with special instructions encoded in the phonorecord or copy for that purpose.
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> "(3) An 'audio recording medium' is any material object, now known or later developed, in any form commonly distributed for use by individuals (such as analog or digital tape cassettes, cartridges or reels), in which a musical work or sound recording can be fixed by use of an audio recording device. Such term does not include a material object that (A) is primarily used for the fixation of motion pictures or other audiovisual works or (B) embodies a sound recording at the time it is first distributed by the importer or manufacturer, unless the sound recording has been so embodied in order to avoid the obligations of subsection (b).
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> "(4) A 'dual audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape

format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one cavity for the insertion of a phonorecord in any such format and one cavity for the insertion of an audio recording medium in any such format. A dual audio recording device does not include any machine or device which is primarily used for reproducing motion pictures or other audiovisual works.

"(5) A 'multiple audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one or more cavities for the insertion of a phonorecord in any such format and two or more cavities for the insertion of an audio recording medium in any such format. A multiple audio recording device does not include any machine or device which is primarily used for reproducing motion pictures or other audiovisual works."

B. Questions Submitted by Senator DeConcini

1. Your testimony today strikes me as very similar to your testimony before this Subcommittee in 1983 in which you predicted the demise of the music industry due to the huge and "ever growing" threat of home taping. Today, however, almost three years after your grim predictions, I read that your industry is enjoying record-high revenues and profits, spearheaded by a host of platinum, multi-mullion selling albums, including Michael Jackson's "Thriller" album which I understand to be the greatest seller of all time. Do you agree that your earlier prediction was far from the mark?

Far from it. My current testimony reinforces my previous testimony in 1983; the harm from home taping continues to escalate. Since 1983, Japan's equipment manufacturers have developed successive generations of dual cassette recorders which are literally personal piracy machines. Further, sales of blank audio tapes continue to escalate, and the use of blank tapes to home tape copyrighted materials -- spurred by tape manufacturer's sales pitches -- continues to flourish. I made "grim predictions" in 1983, and I reiterate them now.

The success of Michael Jackson's album is irrelevant to the widespread harm caused by home taping. It is also totally inaccurate to say that the industry is enjoying "record high revenues and profits." As data submitted to the Subcommittee show, four of the seven companies which accounted for 80% of the industry volume in 1984 sustained losses, not profits, in that year. Overall, for 1984, industry pre-tax profits on domestic operations were only 3.7% of sales. And Dr. Alan Greenspan has estimated that home taping resulted in retail losses of $1.5 billion in 1984 alone. Home taping thus continues to cause massive economic damage.

At bottom, the industry's success in a given year is irrelevant to the misappropriation of copyrighted works that is taking place unabated. In good years or bad, the very equipment manufacturers who oppose home taping legislation enjoy patent, trademark and copyright protection. Even in those years when an industry's profits might be reasonable, or even high, a property right enjoyed by those in the industry should not be diminished. No other industry or business is expected to live with a cap on its earnings potential, or to be the butt of criticism for asserting its right to achieve that potential. The recording industry should not be singled out for such special treatment.

2. I have been reading that the recording industry is having problems producing enough compact disks to

satisfy the huge demand for music in this new format. In fact, Jerry Shulman, a vice president of CBS Records, said last week "it will take a very long time for supply to catch up with demand" (Wall Street Journal, Thursday, October 24, 1985, p. 1). It sounds like you are making the same mistakes with compact disks you made with audio cassettes just three years ago. Why don't you take advantage of these new markets instead of trying to tax the people who create them for you?

Nobody anticipated the incredible popularity of CD players and the resulting demand for compact disks. The record companies are making and will continue to make every effort to meet that demand.

We do not believe, however, that the popularity of CDs has any bearing on the central question now before this Subcommittee: whether copyright owners should be compensated for the proven harm caused by home taping. We are not seeking to tax people who create new markets. Rather, we are seeking compensation from those who profit at our expense when sales of copyrighted material are displaced.

3. On behalf of your industry, you have strongly resisted attempts to label or license allegedly pornographic content of recordings, on the basis that individuals are free to choose the sort of music they wish to support. Tell me, assuming that 10% of the recordings today are of material I find personally objectionable, how can I prevent 10% of the royalty tax I pay on blank tapes and recorders from going to support purveyors of objectionable music? If I wanted to boycott these individuals, wouldn't I have to stop buying blank tape and recorders entirely?

Under the Act, the royalty pool will be distributed among copyright owners in proportion to their share of revenues lost as a result of home taping. Ten percent of your money will not go to people whose music you find objectionable. If such artists get ten percent of the pool, it is only because that is their share of it, based on the number of record purchases that would, but for home taping, have been made by people who do not find their music objectionable. Obviously, then, a boycott of objectionable music will reduce the share of revenues that creators and producers of that music receive under the Act, just as such a boycott now will reduce their share of revenues from record sales.

Such records, in any event, form a very small portion of the number of recordings released. Even groups that have mounted a campaign against objectionable lyrics have acknowledged that the relative number of such recordings is very small. Thus, the assumption that ten percent of recordings today contain objectionable lyrics is not well founded.

4. Mr. Gortikov, how will the monies generated by this proposal be distributed? It is my understanding that the audio copyright owners in this country are not the composers and songwriters but the music publishing companies. Ms. Foreman's testimony indicates that the royalties for the sales and performance of music by John Lennon and Paul McCartney are going to Michael Jackson through his publishing company. Who are these publishing companies?

S. 1739 provides that the money generated by the proposed royalties will be distributed to the owners of the two copyrights encompassed in every recorded tune -- the musical composition and the sound recording. Royalty distributions will be made to all copyright owners of musical compositions and sound recordings that were included in radio or television programs or distributed to the public in the form of records, prerecorded tapes, or other means during the relevant period.

Music publishers are generally the owners of copyrights in the musical compositions; record companies are generally the owners of copyrights in sound recordings. Both groups of copyright owners are obligated by the bill to negotiate in good faith to reach a voluntary agreement on distribution of the royalties; should those negotiations fail to produce an agreement, the bill requires the Copyright Royalty Tribunal to conduct an evidentiary proceeding to determine apportionment of the royalties.

The royalties paid to these copyright owners will, in turn, be shared with others responsible for creating and producing the music on the basis of negotiated contractual agreements. Music publishers will thus share their portion of the royalties with the composers and lyricists they represent; royalties will similarly flow from record companies to recording artists and musicians' and performers' unions.

5. Do you think that the monies generated by this proposal should be distributed on the basis of record sales? Doesn't it stand to reason that the songs most purchased are also those most taped? Wouldn't this result in the rich getting richer and the poor getting poorer? If you favor a system which would distribute the money in any other way, such as subsidies going to classical music or new artists, what would be the rationale for this system in copyright law?

The RIAA believes that the income generated by the proposed royalties should be distributed primarily to compensate copyright owners whose music has been taped, instead of purchased, by consumers. Record sales are a primary indicia that can be used to identify the albums that are most popular and, therefore, quite likely the most taped. Using record sales as the primary basis for royalty distribution would be logical since the compensation is intended to make up for lost sales.

However the music being home taped is identified -- and the CRT is to promulgate detailed regulations for efficient administration of the distribution system -- the RIAA believes, as noted above, that distribution should be based on the fundamental principle that those who are injured because of home taping are the ones who should be compensated by a royalty. As is true of every industry, including those dependent on the labor of artists, successful individuals and entities will no doubt receive more compensation than their less successful counterparts under such a principle. It will not, however, result in the rich getting richer and the poor getting poorer -- all artists, from superstar performers to backup musicians, will benefit from enactment of S. 1739, since it will enable them to recoup at least some portion of the revenues they are losing to the home taping menace.

Indeed, even those who have not yet had recordings made of their work -- and who therefore will not directly receive home taping royalties -- will benefit from this legislation, for it will generate sorely needed revenues to underwrite new performers, new songwriters, new musicians and new music. The music industry has traditionally relied upon the revenues generated by its few hits to support the investment required for tomorrow's generation of creators -- an investment which is entirely consistent with, and indeed furthers, the principles of copyright law. As Beverly Sills once testified before this Subcommittee, it was the success of the Beatles that enabled her record company to finance her operatic recordings.[14]

Thus, for the less established, less popular, or less successful artists, the infusion of revenues from home taping royalties means renewed opportunities and brightened prospects for a career in music. It is not at all surprising, therefore, that the aspiring songwriters, performing artists and musicians of America are so solidly in favor of this legislation. In fact, representatives of working people throughout the country understand that enactment of the proposed royalty will redound to their benefit. The AFL-CIO has recently announced its support for S. 1739 because it enables "performers, writers, technicians and crafts people who produce sound recordings" to be fairly compensated for the use of their work.[15]

6. We have here the statement of Mr. Feldman that it is technically impossible to distinguish audio and video for the purposes of this legislation. Especially when the two technologies are merging into one, how can the problem of taxing video recorders and video tape be avoided?

The music community does not seek to include video recorders and tapes in the royalty system created by the bill. To remedy any ambiguity in the Act, the music community proposes the following changes in Section 119(d). Changes from current language are underscored.

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[14] Copyright Infringements (Audio and Video Recorders): Hearings Before the Senate Comm. on the Judiciary, 97th Cong., 1st and 2d Sess. 441 (1981 & 1982).

[15] See "Preserving the American Copyright System and Jobs in the Performing Arts," AFL-CIO Resolution No. 250 (November 1985).

"(2) An 'audio recording device' is any machine or device, now known or later developed, which can be used for making audio recordings by individuals for private use, and which is capable of reproducing the sounds embodied in a radio or television transmission, or in a phonorecord or copy, by means of internal or external wire, cable or like connection between the equipment receiving or performing such sounds and the equipment reproducing them. The term 'audio recording devices' includes dual audio recording devices. Such term does not include a device (A) which is primarily used for reproducing motion pictures or other audiovisual works; (B) which is unable to receive the sounds embodied in a radio or television transmission, or in a phonorecord or copy, except by microphone; (C) which is capable only of performing such sounds (playback only equipment); or (D) which incorporates a decoder or similar mechanism that prevents the device from reproducing, or permits the device to reproduce, the sounds embodied in a phonorecord or copy in accordance with special instructions encoded in the phonorecord or copy for that purpose.

"(3) An 'audio recording medium' is any material object, now known or later developed, in any form commonly distributed for use by individuals (such as analog or digital tape cassettes, cartridges or reels), in which a musical work or sound recording can be fixed by use of an audio recording device. Such term does not include a material object that (A) is primarily used for the fixation of motion pictures or other audiovisual works or (B) embodies a sound recording at the time it is first distributed by the importer or manufacturer, unless the sound recording has been so embodied in order to avoid the obligations of subsection (b).

"(4) A 'dual audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one cavity for the insertion of a phonorecord in any such format and one cavity for the insertion of an audio recording medium in any such format. A dual audio recording device does not include any machine or device which is primarily used for reproducing motion pictures or other audiovisual works.

"(5) A 'multiple audio recording device' is any machine or device, now known or later developed, intended for use in private homes, which can be used for making audio recordings by individuals for private use, which is capable of reproducing the sounds embodied in a phonorecord by copying such sounds from a phonorecord in any digital or any tape format to an audio recording medium in any digital or any tape format, and which contains in a single apparatus one or more cavities for the insertion of a phonorecord in any such format and two or more cavities for the insertion of an audio recording medium in any such format. A multiple audio recording device does not include any machine or device which is primarily used for reproducing motion pictures or other audiovisual works."

C. Questions Submitted by Senator Leahy

1. The bill provides for exemptions from royalty fees for particular kinds of "audio recording media" if they are unsuitable for making recordings for private use.

What are some examples of media which would be covered by this exemption?

Tapes currently promoted and sold for use in dictation machines, for taping speeches and lectures and for telephone answering machines are examples of "audio recording media" that would not be deemed suitable for the taping of copyrighted material.

2. Critics of this bill have said that more than half of the total tapes recorded at home contain something other than prerecorded copyrighted music. Is this true, and if so, are there exemptions in this bill to cover these noncopyrighted uses?

Opponents of home taping legislation have argued that over half of all home taping involves no prerecorded music. Putting to one side the issue of whether this assertion is even accurate, it is not, in any event, a relevant statistic. Rather, the question is what percentage of tapes contains copyrighted material. Based on an actual examination of tapes in people's homes, Audits & Surveys found that at least 84% of home tapes are used to tape prerecorded music.[16]

Moreover, the Act goes to great lengths to insure that the small percentage of tapes or equipment used for noninfringing purposes will be exempt from royalties. It provides, first, that no royalty is to be imposed on tapes or equipment used for commercial, professional, educational or similar purposes. Second, the Act limits the royalty on tapes to those that are suitable for music recording, and specifically exempts from royalties tapes that are -- based on certain technical criteria -- "unsuitable" for music recording. Such exemptions may not achieve a perfect fit; there may remain a tiny fraction of total tapes that bear a royalty but that are never used to record music. It is far more likely, however, that there will be a large number of tapes that are exempt from the royalty but are nonetheless used to record music. In any event, rejecting the overall legislation because the solution is not perfect would perpetuate a far greater inequity: the denial of any compensation at all to those injured by home taping.

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[16] The explanation for the apparent discrepancy is that nonmusic taping is often done over and over again on the same tape. Unlike tapes that consumers make of prerecorded music, tapes containing dictation, phone messages, and class lectures are not saved and enjoyed for a period of years.

3. Critics of this bill have said that the number of claimants involved, the lack of any agreed-upon method for measuring the amount of home taping either in the aggregate or for particular songs, and the bill's lack of criteria to guide the distribution process, will result in lengthy and intrusive litigation before the CRT over the amount each claimant should receive.

Do you agree? If not, why not?

We do not agree that S. 1739 will result in "lengthy and intrusive" litigation over distribution of the proposed royalties. First, it is quite possible that there will be no litigation before the CRT at all; the bill obligates all those copyright owners who have filed claims (or their chosen representatives) to negotiate in good faith among themselves to reach a voluntary agreement on the distribution of the royalties. If such an agreement is reached, the CRT's role in the distribution process will be minimal: approving and implementing the agreed upon distribution.

Even if the CRT does become involved in apportionment of the royalties, moreover, the mechanisms in the bill -- which build upon and extend existing and successful copyright administration systems -- ensure the smooth functioning of the distribution process. The CRT is an existing government agency which has developed considerable expertise in the conduct of formal royalty distribution proceedings: it administers distribution of the royalties paid to copyright owners of works performed on jukeboxes and cable television systems. In addition, the CRT may employ existing systems and data bases that can provide the necessary criteria for distribution of the royalties. ASCAP and BMI, for instance, regularly prepare data on radio and television performances of musical works to aid in distribution of performance royalties, and The Harry Fox Agency and record companies maintain data on sales of records and prerecorded tapes. The CRT may alternatively commission surveys designed to determine the number of tapes that are made of each album released.

The collection and distribution of royalties in the world music industry have been proceeding for decades, both in the United States and abroad. There is thus no reason to think that the process will not work smoothly in this instance. Congress is, however, of course free to create additional standards and guidelines that will respond to any concerns over the distribution system as proposed.

4. According to the proponents of this bill, in 1984 more than $1.5 billion of actual album and prerecorded tape sales were displaced by home taping.

What percentage of that amount would have gone to songwriters if there had not been any displacement by home taping?

If this bill had been in effect in 1984, what portion of that $1.5 billion would have been replaced by royalties from tapes and audio equipment?

What percentage of that amount (generated by royalties) would have gone to songwriters?

Dr. Alan Greenspan has estimated that the actual loss sustained by the music industry in 1984 as a result of home taping amounted to approximately two-fifths of the $1.5 billion in retail sales losses.[17] Of that amount, some $60 million or more would have been paid to songwriters and their music publishers had there not been any displacement by home taping.

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[17] See Testimony of Alan Greenspan Re: S. 1739, Before the Subcommittee on Patents, Copyrights and Trademarks, Senate Comm. on the Judiciary at 12 (October 30, 1985).

If S. 1739 had been in effect in 1984, songwriters and their music publishers would have received at least partial compensation for these losses. Dr. Greenspan has estimated that the royalties proposed in the bill will yield about one-third of the music industry's actual losses, or approximately $200 million. Of this $200 million, the actual amount that would have been paid to songwriters would have been determined by the Copyright Royalty Tribunal or by the parties pursuant to negotiation.

5. Critics of this bill assert, contrary to claims by the music industry, that creative and artistic output is very high in the music community. They point to the emergence of many new female country singers, among others.

The industry says that home taping is one reason why the number of new albums has fallen by more than half since 1978.

Do you agree that creative output of music is high?

If not, what happened to the $4.4 billion in record industry profits in 1984?

If those kinds of profits were not used to encourage creative output, why will the revenues from this bill result in investment in new music?

With the exception of a few stars, the period during which most performers' albums achieve commercial success is pitifully brief. The continued infusion of new talent is thus imperative for survival of the music industry, and record companies devote as much of their revenues as they can to the development of new music. To the extent, however, that home taping diminishes sales revenues -- which it does to the tune of approximately $1.5 billion each year -- it depletes the resources record companies would otherwise invest in this development. Accordingly, as the data on releases demonstrate, creative output is not as high as it would be if recording companies received compensation for the sales displaced by home taping; with such compensation, perhaps the list of new female country singers would be twice as long as it is today.

There were no $4.4 billion in record industry profits in 1984; indeed, as Dr. Alan Greenspan has testified before this Subcommittee, profits in the industry remain depressed, in large measure as a result of home taping. Estimated retail sales, calculated at list prices, were approximately $4.4 billion; according, however, to data submitted to this Subcommittee, and as discussed at greater length at the beginning of this submission, the U.S. sales operations of seven companies analyzed by Touche-Ross had an operating profit of only 3.7%.

6. The bill provides for an exemption from tax for tape that is not suitable for making audio recordings "on the basis of technical criteria."

What are the criteria?

Can't a low quality tape used by one person to record a lecture be used by another to record music?

Right now, each manufacturer of blank tape distinguishes among various grades of tape it produces, advertising some as suitable for recording certain types of music, others as suitable for recording music from certain sources such as CDs and still others as suitable for recording voices. In reliance upon these marketplace representations, the bill includes provisions to distinguish tapes on the basis of technical criteria. Manufacturers who have promoted these distinctions for years can assist the recording industry and other experts in refining the criteria and in identifying specific types of tapes that are unsuitable for recording music. Congress could, in addition, provide other means by which royalty-bearing and non-royalty-bearing tapes can be distinguished: for instance, tapes of less than a certain length, or sold for less than a certain price, could be exempted from a royalty.

The fact that a low quality tape can be used to record music is exactly why the Act bases the exemption on suitability instead of capability. Anyone who tapes an album onto a cassette that is not suitable for such taping will indeed have a tape of the album, but it will be one of inferior quality. For this reason, we believe it fair to assume that the taping of an album on a tape not suitable for that purpose is not likely to displace a sale.

7. Critics of this bill say that prerecorded music, taped at speeds up to 64 times real time, is inferior to music taped at home in real time.

How much home taping is done not to avoid buying records but to get the best quality portable music?

The purpose of this criticism must be to suggest that the predominant reason that people tape is to get better quality recordings and not to avoid buying prerecorded music. In fact, statistics demonstrate the opposite: far more people tape to save money and to avoid buying records than to get better quality. The survey performed by CBS shows, for instance, that more than twice as many respondents said that their primary reason for taping was to save money than said that they taped primarily to get better quality.[18] And WCI found that only 3 percent of respondents indicated that they taped most frequently to make tapes of better quality than prerecorded cassettes.[19]

It is, in any event, untrue that consumers need to home tape to get better quality cassettes. Record companies are now using very high quality tape for their prerecorded cassettes, and many releases are being recorded on metal and premium brands of tape. Recording industry studies show, furthermore, that consumers recognize this improvement and agree that the quality of prerecorded cassettes available today is markedly better than it used to be.

8. How many audio tapes are sold in this country each year that will be subject to the 1¢ per minute tax?

Dr. Alan Greenspan has estimated that, if S. 1739 were enacted, approximately 128 million premium quality tapes would be sold bearing a royalty.[20] This is fewer than half of the 261 million tapes that were sold in the United States in 1984.[21]

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[18] CBS Records, "Blank Tape Buyers: Their Attitudes and Impact on Prerecorded Music Sales," at 11 (Fall 1980).

[19] Warner Communications, Inc., "A Consumer Survey: Home Taping," at 17 (March 1982). Both the CBS and WCI surveys have been previously submitted to the Judiciary Committee. See Copyright Infringements (Audio and Video Recorders): Hearings Before the Senate Comm. on the Judiciary, 97th Cong., 1st and 2d Sess. 775-826, 848-864 (1981 & 1982).

[20] Nonpremium tapes were excluded from this calculation on the ground that they are likely to be exempt from royalties under S. 1739.

[21] See Merchandising Magazine, March 1985 at 94.

9. How much income will be generated each year from the royalties from the sales of just audio tapes?

Dr. Greenspan has estimated that the royalty on tapes will yield approximately $106 million each year.[22]

10. Isn't the decrease in the number of new record releases since 1978 due to the industry's decision that it is more profitable to put their money into fewer artists who have proven successful, like Michael Jackson and Bruce Springsteen?

In 1983, 1984, and 1985, the labels for which Michael Jackson and Bruce Springsteen record certainly profited from their success. Undoubtedly, both are "proven successes" today. Without risk-taking by record companies, however, there would be no such "proven successes."

Five out of every six albums released fail to cover their costs. At some point -- and not all that long ago -- Bruce Springsteen was known only to devotees of the boardwalk in Asbury Park, New Jersey; also not very long ago, Michael Jackson was trying to establish himself as a solo performer, no longer just one of the Jackson Five. In both cases, there was absolutely no assurance that their records would turn a profit.

A recording industry in which a few top stars provide all or almost all of the profit margin is not in anyone's interest. The satisfaction of consumers, the creativity of artists and the security of record companies would be greatly enhanced if compensation for sales displaced by home taping was provided. That way more new talent -- still commercially unsuccessful or only marginally successful -- could be given the opportunity to develop into "proven successes."

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[22] See Table 8, "Estimated Yield of Blank Tape Royalty," submitted to this Subcommittee with Dr. Greenspan's testimony on S. 1739.

11. Since 1982, proponents of this bill have said that the continued free home taping of copyrighted music threatens the industry's existence and hurts the public.

The price of music will increase -- there will be less investment in new and less popular music, and less incentive to create music.

Opponents point out that people have been taping music at home for years, but in 1984 the recording industry had its best year ever, with revenues of almost $4.5 billion.

In the past two years, while home taping has been increasing, has there in fact been less investment in new music and less incentive to create music?

The recording industry's estimated retail sales, calculated at list prices, of $4.4 billion in 1984 are far greater than record companies' wholesale revenues, which were about $2.2 billion that year. Most important, these revenue figures do not change the fact that a majority of companies failed to achieve a profit that year. According to data analyzed by Touche-Ross and provided to this Subcommittee, the seven major companies that provided information -- which together accounted for 80% of record sales in the United States that year -- had a pre-tax operating profit of only 3.7% of sales. The depressed profit margins in the industry, largely attributable to home taping, mean that record companies have less money to devote to the necessary task of developing new talent and music. In short, the increase in revenues, by itself, has very little bearing on the ability of record companies to invest in new music and to provide adequate incentives for those who create it.

12. According to the Recording Industry Association of America, the number of new albums released has fallen by almost half since 1978.

Why has this happened during a period of record profits for the industry?

Can home taping really be blamed for this?

What kinds of titles have been dropped?

This is not "a period of record profits for the industry." This is, rather, a period during which the industry has gone from an extremely unprofitable posture to one in which profits are still significantly depressed and give every indication of remaining that way. These depressed profit margins have reduced the amount of money that record companies have available to invest in less commercially viable music, and have caused the drastic decline in the number of new releases.

Home taping is not the only cause of the low profits, and hence of the decline in releases; all available evidence, however, shows that the massive amount of home taping now going on has resulted in displaced sales and consequently, in lost revenues and profits. Indeed, Dr. Greenspan has estimated that home taping resulted in losses of $1.5 billion in sales revenues in 1984 alone.

The need to cover their short-term costs puts pressure on record companies to put out albums that will have widespread commercial appeal. The types of music least likely to achieve widespread commercial success -- classical music, jazz, music with a specific ethnic or cultural appeal -- are the ones most threatened as a result of the industry's low profitability.

13. When the New York Philharmonic Orchestra makes a record today, how are the profits from that album distributed?

How much goes to the orchestra? How much goes to the record company? How much goes to the composer? How much goes to the music publisher?

When the New York Philharmonic Orchestra makes a record today, the record company for which it records distributes revenues to the orchestra, and pays royalties to the composer and the music publisher when the musical work recorded is not in the public domain.[13]

Music publishers and composers are compensated by means of the mechanical royalty, which is paid to publishers by record companies for the use of musical compositions. Mechanical royalties are paid on a flat rate basis for each musical composition on each sound recording sold: the rate will increase on January 1, 1986 to 5 cents per selection or .95 cents per minute of playing time, whichever is larger. That royalty is shared by the music publisher and the composer; songwriters customarily receive 50 percent of the royalty rate.[14]

Determining the amount that will be paid to the orchestra and the record company is more complex. Often, the record company will pay a contractually negotiated amount to the orchestra, which will then, on the basis of its own contractual arrangements, reimburse its members directly as employees. Alternatively, featured soloists (as in a piano concerto) may negotiate to receive contractual royalties -- i.e., a set percentage of the recording's wholesale or suggested retail price; union performers may be paid by a flat fee set by their unions. Union members may also receive the benefit of contributions that record companies are obligated to make to union funds created to support musicians and disseminate their music to the public. Such contributions are made on the basis of record sales. Thus, about .35 of 1% of the list price of each record sold is contributed to the Music Performance Trust Fund, which collects $10-$18 million annually to hire union musicians to perform in free public concerts presented in 550 U.S. communities. An additional .6 of 1% of the price of each record sold goes into the Special Payments Fund maintained by the American Federation of Musicians to be distributed as additional payments to those musicians who have performed in recording sessions at regular session rates.

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[13] The sale of a record by the New York Philharmonic results in the distribution of revenues, not profits. Record companies do not make a profit on their releases until a sufficient number of albums is sold to cover the costs of producing the recording. This happens rarely: as industry studies show, five of every six albums released fail to cover their costs.

[14] As previously indicated, if the music used is in the public domain -- if, for instance, it is a composition by Bach or Beethoven -- then it is not protected by copyright, and record companies need not pay mechanical royalties for the use of it.

A record company cannot profit from sales of a record until it has recouped all of the costs of producing that record -- including the costs of manufacturing and production and the overhead expenses incurred to support the infrastructure necessary for continued music production. Notwithstanding its hopes for an adequate return on each album it produces, a record maker thus enjoys no profit until it has sold a sufficient number of albums to cover its costs. In fact, the record business is an exceedingly risky one: according to RIAA industry studies, five out of six records released fail to cover their costs.[25] As home taping displaces sales, therefore, it diminishes the likelihood that the recording industry will ever be able to recoup its costs from music production.

14. Are profits distributed the same way whether the musician is Michael Jackson, the New York Philharmonic, or a little known guitar player from Vermont?

If the amounts distributed differ according to contract, what would be a reasonable guess of how these profits would be distributed if Michael Jackson were the musician?

As noted previously, revenues from sales of a record are distributed to participating artists on the basis of contractual negotiations between the artist and the record companies. Featured performers or groups typically negotiate to receive as royalties a percentage of the wholesale or suggested retail price of albums. Those royalties typically run anywhere from 22 percent to 36 percent of the wholesale price, and the amounts may increase when a threshold level of record sales is reached.[26] It is reasonable to expect that Michael Jackson's share right now would be at the high end of this range.

Back-up musicians and vocalists are generally paid by a flat fee set by their unions. They too, however, benefit from increased sales of records in which they have participated, since the record company is obligated to contribute a portion of the list price of each record sold to union funds created to support musicians and disseminate their music to the public.

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[25] "Economic Study of the Recording Industry," Cambridge Research Institute, April 7, 1980, at 9.

[26] Featured performers may alternatively receive a guarantee that they will be paid a set amount regardless of how many of their albums are sold. These amounts are also determined by contract.

Thus, representatives of musicians and vocalists, as well as other working people throughout the country, understand that enactment of the proposed royalty will redound to their benefit. The AFL-CIO has recently announced its support for S. 1739 because, by providing additional revenues for copyright owners, it enables "performers, writers, technicians and crafts people who produce sound recordings" to be fairly compensated for the use of their work.[27]

15. Under this bill, royalty fees would be deposited in the Copyright Office and then transferred to the Treasury Department. How will these royalties be distributed?

How much will go to the various copyright owners?

Under the Act, copyright owners are entitled to share in the proposed royalties if their musical works or sound recordings were played on the radio, broadcast on television, or sold in the form of a record or prerecorded tape during the year for which the royalties are collected. As currently provided in S. 1739, distribution of these royalties will be overseen by the CRT.

The bill provides that the CRT will become involved in apportionment of the royalties only if copyright owners, negotiating in good faith among themselves, are unable to reach a voluntary agreement on royalty distribution. If such an agreement is reached, the Tribunal will deduct the reasonable costs of administering the royalty from the royalty pool and distribute the royalties based on the claims filed by the copyright owners.

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[27] See "Preserving the American Copyright System and Jobs in the Performing Arts," AFL-CIO Resolution No. 250 (November 1985).

If such an agreement is not reached, the bill provides that the Tribunal is to conduct an evidentiary proceeding to determine apportionment of the royalties among copyright owners. The Tribunal may refer to existing data bases -- compiled, for instance, by ASCAP, BMI, The Harry Fox Agency and record companies -- that have been used to assist distribution of performance and mechanical royalties. The Tribunal may, alternatively, commission surveys designed to determine the number of copies made of each album released.

The royalties paid to the copyright owners will, in turn, be shared with others responsible for creating and producing the music on the basis of negotiated contractual agreements. Thus, composers, lyricists, recording artists, back-up musicians and vocalists will all benefit from distribution of the proposed royalties.

16. How much of the royalties generated by this bill will actually be used by record companies to underwrite new performers?

How much will be used to subsidize less profitable forms of music such as classical and jazz?

Record companies have always devoted as much of their sales revenues as they could to the development of new music. Because virtually every recording released has a brief sales life, and because even star artists do not permanently retain their popularity, it has been important for the very survival of the record companies that they continue to cultivate and promote new talent. Moreover, to the extent they can, record companies want to continue to provide the diversity of classical, jazz and other recordings the music community has been able to produce in the past.

Home taping siphons off the revenues that the music community has traditionally used to support these worthy goals. Enactment of S. 1739 will replace a portion of those revenues and will in some measure restore the ability of record companies to take chances on new talent and more specialized types of music. We believe, based on past practices and the interest of the record companies in promoting new talent, that support for the development of new performers or less profitable forms of music will be ample.

17. It has been estimated that the average tax per tape under this bill will be 78¢. This will result in an increase in price of 74%. Most of this cost will be passed on to consumers.

What is the basis for the amount of the tax -- 1¢ per minute on blank tape?

What is the relationship between the amount of the tax, and the amount of home taping or the damage caused by home taping?

Where did the 5% and 25% taxes on audio recorders and dual cassette recorders come from, that is, why 5% rather than 1% or 10%?

The royalty rates proposed in the Act are designed to serve two fundamental goals: reimbursing the music community for some portion of its losses due to home taping, and insuring that rates are kept as low as possible. The rates proposed in the Act represent an equitable approach to these two objectives: they are the lowest rates that can be set that would nonetheless generate some meaningful compensation for the music community.[28]

Indeed, the royalty rates proposed in the Act are so low that they will not even come close to making creators and copyright owners whole for the losses they incur as a result of home taping. Dr. Greenspan has estimated that the music industry's net loss due to home taping -- excluding those of its costs that are not incurred because of reduced sales -- is approximately $600 million annually. He has further estimated, however, that the royalties proposed in S. 1739 will yield about $200 million each year -- only about one-third of actual losses. This estimate is based on his calculation that 128 million premium quality tapes would be sold bearing a royalty, and that the amount thereby generated would be approximately $106 million. The balance of the compensation yielded would be made up by royalties on equipment.

These calculations demonstrate one of the reasons that equipment is included in the royalty system: to insure that meaningful sums can be collected while royalty payments on tapes are kept as low as possible. If royalties were to be paid on blank tape only, the higher fee required to realize even this partial compensation would place a disproportionate burden on blank tape sales.

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[28] It is not at all certain that consumers will in fact pay the full amount of the royalties. Competitive factors in the marketplace may lead importers and manufacturers to absorb the royalty -- or some portion of it -- as a cost of doing business, rather than passing it through to their customers.

But there is another reason that royalties must be assessed on equipment as well as tape: the inescapable link, emphasized again and again by equipment manufacturers, between recording devices and the home taping of music. A higher rate has been set for dual cassette machines, moreover, because these recorders are specifically designed to facilitate home taping -- to be personal piracy machines.

The music community welcomes suggestions from the blank tape and equipment industries about more appropriate rates that might nonetheless reimburse the music community for a reasonable portion of the revenues it now loses to home taping. To date, however, representatives of these industries have refused even to acknowledge that a problem exists, much less to join in consideration of an equitable solution.

18. Would a student who tapes his physics class lecture have to pay a royalty on the tape?

What about a parent who tapes her ten-year-old daughter's piano recital?

What about tapes for telephone answering machines?

Does this bill provide for exemptions for these types of uses?

It is not our intention to recover royalties beyond those that compensate for displaced sales of prerecorded music. The Act as now drafted would prevent the overbroad imposition of a royalty: tapes not suitable for taping prerecorded music, but rather intended to be used for noninfringing purposes -- such as taping lectures or phone messages -- would not bear any royalty.

Currently, the Act bases the suitability determination on technical criteria that are to be set and applied by the Copyright Royalty Tribunal. If Congress so desired, in addition to or instead of this procedure, it could exempt other categories of tape. For instance, tapes of less than a certain length (e.g., 30 minutes) or tapes that cost less than a certain amount could be exempted.

Those using full-length premium quality tapes to record piano recitals -- and not purchasing such tapes from music schools or instructors, who may claim the Act's exemption for professional activities -- would be among the tiny minority of tapers who would pay a royalty for noninfringing activities. But rejecting the overall legislation because of such an imperfection would perpetuate a far greater inequity: the denial of any compensation at all to those injured by home taping.

Touche Ross & Co.

October 19, 1985

Mr. Stanley M. Gortikov, President
Recording Industry Association of
America, Inc.
888 Seventh Avenue
New York, New York 10106

Dear Mr. Gortikov:

At your request, we have performed the procedures enumerated below in connection with your survey of estimated financial statistics for U.S. recording companies, 1981-1984. Our work was done solely to assist you in accumulating estimated financial statistics, which we have summarized in the attached schedules. The form for reporting the requested information was prepared by you, as was the mailing to RIAA member companies, with instructions for them to return the completed forms directly to us.

The procedures we performed are summarized as follows:

1. A control list was maintained noting the date each completed form was received and the name of the company responding. Although all forms were due by June 24, 1985, the last form was received on September 20, 1985. During this period, we provided you with periodic updates concerning data we received.

2. A code number was assigned to each response form received to ensure confidentiality, with a separate file maintained containing the corresponding company names. We did not provide or disclose individual company data to RIAA or any of its member companies.

3. We read the response forms to ensure that the requested information had been completed.

4. Based on your instructions, the attached survey of estimated financial statistics for U.S. recording companies, 1981-1984 was compiled utilizing the data received from reporting companies.

Because the above procedures were not sufficient to constitute an examination made in accordance with generally accepted auditing standards, we do not express an opinion on any of the specific amounts included in the attached survey. Further, we make no representations as to the sufficiency of the foregoing procedures for your purposes. With respect to the procedures referred to above, no matter came to our attention that caused us to believe that the amounts in the attached survey should be adjusted.

Very truly yours,

Touche Ross & Co.

Certified Public Accountants

1985 FINANCIAL SURVEY OF RECORDING INDUSTRY

(1981 - 1984)

	Year ended			
	1981	1982	1983	1984
	(000's omitted)			
1. Net sales	$1,561,662	$1,407,580	$1,547,082	$1,754,476
2. Cost of goods sold:				
a. Contributions to artists' funds	12,241	9,739	9,991	10,665
b. Unrecoupable flat payments to artists	6,592	5,336	4,081	3,391
c. Unrecouped advances to artists	104,560	86,024	89,350	66,612
d. Artists' royalties	286,037	262,274	292,920	336,614
e. Other talent costs and recording expenses	26,867	18,390	15,467	18,800
f. Copyright mechanical royalties	90,238	87,618	98,219	113,030
g. Production and manufacturing	451,531	398,358	407,663	446,038
h. Total cost of goods sold (a-g)	978,066	867,739	917,691	995,150
3. Gross margin (1-2)	583,596	539,841	629,391	759,326
4. Sales and promotion expenses	415,623	417,235	413,266	472,907
5. General and administrative	227,872	227,375	223,224	247,064
6. Miscellaneous income:				
a. Record related revenues*	14,433	14,233	9,793	17,165
b. Unrelated revenues	18,258	9,251	6,473	8,895
c. Total miscellaneous income (a+b)	32,691	23,484	16,266	26,060
7. Profits before income tax (3-(4+5)+6)	$ (27,208)	$ (81,285)	$ 9,167	$ 65,415
*Memo item:				
Gross video sales	$ -	$ -	$ -	$ 9,518
Less all video-related costs	1,400	1,100	2,900	12,773
Video sales net of expenses	$ (1,400)	$ (1,100)	$ (2,900)	$ (3,255)
Number of participating companies	6	6	7	7
Number of companies showing a profit	3	-	1	3
Number of companies showing a loss	3	6	6	4

Notes:

(1) The above figures do not contain information from Chrysalis for 1981 and 1982.

(2) Figures for Capitol Records were provided on March 31 fiscal year basis, with 1980 figures including nine months of data.

(3) CBS included "Other Talent Costs and Recording Expenses" (2e) with "Unrecouped Advances to Artists," (2c), as specific information was unavailable, and also included Label A & R and "All Other" miscellaneous information.

1985 FINANCIAL SURVEY OF RECORDING INDUSTRY

(1981 - 1984)

DISTRIBUTED LABELS OF PARTICIPATING COMPANIES

(December 31, 1984)

ARISTA

Arista
Buddah
Jive

CAPITOL

Accord
Angel
Apple
Blue Note/Liberty
Capitol
Capitol Int'l
EMI-America
Gold Coast
Harvest
Imperial/Liberty
Liberty
  (formerly UA)
Main Street
Montage
Melodiya/Angel
Seraphim
Spector

CBS

Columbia Group:
  ARC
  Columbia
  Columbia/Cleveland
    Int'l
  Columbia/Enter-
    tainment Co.
  Columbia/415
  Tappan Zee

Epic Group:
  Epic
  Epic/Cleveland
    Int'l
  Full Moon/Epic
  Portrait
  Portrait/Lorimar
  Stiff/Epic
  Virgin/Epic

Masterworks

CSP

Associated Group:
  BID
  Bobcat
  Boulevard
  Caribou
  Carrere
  CBS Associated
  Chicago Int'l
  Curb
  Estate
  Jet
  Johnson
  Kat Family
  Kirshner
  My Disc
  Nemperor
  Pasha
  PIR
  Scotti Bros.
  Silver Blue
  Tabu
  T-Neck
  TSOP

CHRYSALIS

Chrysalis

POLYGRAM

Atlanta Artists
Carrere/America
Casablanca
Chocolate City
Compleat
Deram
Deutsche Grammophon
E-lite
Emarcy
Enja
Gramavision
Lection
Limelight Jazz
London
London Int'l
London Phase 4
London Treasury
Mercury
Millennium
MPS
Musical Zodiac
Musikfest/DG
Oasis
Parachute
Philips
Philips Cassettes
Polydor
Polydor (MGM)
Riva
RSO
Threshold
Total Experience
11
Vertigo
Verve

RCA

Ariola America
Bluebird
Camden
Erato
Grunt
Plant
Regard
RCA
RCA Int'l
Salsoul
Total Experience
Victrola
Wave

WCI

Warner Bros. Group:
  Bearsville
  Dark Horse
  Deep Purple
  ECM
  Full Moon
  Geffen
  Island
  Qwest
  Reprise
  Sire
  Slash
  Warner Bros.
  Warner/Curb
  Whitfield

Elektra/Asylum Group
  Asylum
  Beserkley
  Elektra
  Elektra/Musician
  Nonesuch
  Solar

Atlantic Group:
  Atco
  Atlantic
  Big Tree
  Capricorn
  Cherie
  Cotillion
  Embryo
  Emerald City
  Esperanza
  Finnadar
  Little David
  Manticore
  Mirage
  Modern
  Radio
  Regency
  Real World
  Rolling Stones
  Swan Song
  Syntonic Research

Mr. GORTIKOV. Our next witness is Mr. George David Weiss, who is the president of the Songwriters Guild of America.

STATEMENT OF GEORGE DAVID WEISS

Mr. WEISS. Thank you, Stanley, and thank you, Mr. Chairman, for this opportunity.

My name is George David Weiss, president of the Songwriters Guild of America. We have about 5,000 members in all 50 States.

Now, in this position my salary is zero, but I sure hope you will not hold that against me. I guess I was 7 or 8 years young when I first heard the expression "I bought it for a song." I soon realized it was another way of saying it was cheap or it almost cost nothing.

When I became a professional songwriter, the full implication of that cliche hit me. It seems that people always figured that songs belonged to everyone. Anybody could use them, sing them, write parodies on them. After all, there was nothing solid in a song. You could not touch it or hold it. Of course, it was free.

Then I came face to face with the royalties paid to songwriters. What with statutory rates, compulsory licenses and earnings which depend upon the sale of one copy of a record and another and hopefully another, et cetera, pennies, it is clear that writers have never had a gushing fountain from which to drink.

Oh, sure, there are some singer-songwriters who have large incomes, but, you see, even they don't earn it from their songs; they make most of it from their in-person performance. The vast majority of us compete with each other for our songs to be included in an album. Then we hope and pray it will sell.

Most of us just earn a living. Sometimes more, often less. Now, if I entered a lamp shop and said, "Oh, what a gorgeous lamp! I am taking it home now, free," you know what would happen? Sirens, police, jail! My wife would have to bail me out.

But, you see, Mr. Chairman, people are taking my product home free every day. They tape off the air, from records borrowed from a friend, or like some college kids are doing, they form a club, buy a few LP's a month, or borrow them, and make copies for all members of the group, all for free.

Now, even though my songs are copyrighted, and they are the property of my publisher and myself, I get nothing. Not 1 red cent in royalty when my creation is taped. But the importers, the manufacturers, the sellers of blank tapes and recorders, they earn, you bet! And the bitter irony is they will have no such multibillion dollar industry if not for the works and music of my peers and myself.

The very fact that the public is taping my songs certainly indicates that they like what I wrote. Don't I deserve something for having brought them pleasure? Don't I deserve an economic incentive to continue contributing to the common good as urged by our Founding Fathers?

It is entirely possible that if we continue this headlong dash into creative oblivion, I will face great difficulties in meeting my financial obligations, sending my boy to college, paying my mortgage and my bills. And it saddens me to even contemplate finding another way of earning a living at this stage in my life.

I guess I could be a shoe salesman, but I was born with a song in my heart, not a shoe, and I think I have earned the right to continue doing what the good Lord intended me to do; that is, writing songs like "Mr. Wonderful," "Too Close For Comfort," "Lullaby of Birdland," "The Wheel of Fortune," "Cross Over the Bridge," "The Lion Sleeps Tonight," "Oh What It Seemed to Be," "What a Wonderful World," "Bette Midler's Stay With Me," "Elvis' Theme Song," and "Wise Men Say."

When I and my colleagues are put out to pasture, either by age or blank tapes, what about tomorrow? Who will enter our profession and become the new talented exciting writers of America when we guarantee them in advance that they will not earn an adequate living? No, they will probably go into business selling blank tapes and audio cassette recorders and do a lot better; that is, if there is any music left to be recorded by then.

I urge this committee and this Congress to pass S. 1739 and prevent the already pejorative connotation of "I bought it for a song" from being mutated into "I taped it for free."

Thank you.

[Following responses were subsequently submitted for the record:]

RESPONSES OF GEORGE DAVID WEISS
TO QUESTIONS SUBMITTED BY SENATOR DECONCINI

Question 1

A. Could you explain to me who owns the copyright for most music and therefore who would be receiving the monies collected under this proposed legislation?

One must understand the nature of the relationship between songwriters and music publishers to answer this question.

From 1909 through the late 1950s the vast majority of songwriters would enter into an agreement with a music publisher under which they would assign their copyright. In exchange, the music publisher would pay to the songwriters stipulated royalties. Those royalties varied considerably. While today's industry's standards, as a general rule, provide for an even division of royalties between the publisher (50%) and the composer and lyricist (50%) this was not the case in the early days of music publishing where the publisher, in addition to paying the writers between 2¢ and 3¢ for each copy of sheet music sold (which was an important market in that period) would pay the writers approximately 33 1/3% of other revenue retaining the rest for themselves. (The forgoing excludes payments by the 3 performing rights societies which are paid directly to writers and publishers).

Starting in the late fifties and early sixties, certain things occurred: with the strength of The Songwriters Guild which has been the leader in the field we were able to bring about an even division of mechanical royalties, synchronization royalties and like uses between the publisher on the one hand and the songwriters on the other. In addition the royalties paid on sheet music was increased substantially. In all of these cases the monies were paid directly to the music publisher, since the copyright had been assigned to the music publisher, and the flow of monies (excluding performing rights proceeds) followed the copyright.

Also, another radical change occurred in the industry, particularly with the advent of the singer/songwriter. In addition to recording their own performances they also authored their own copyrights. They entered into direct agreements with record companies who would pay the singer for his or her performance; and would pay all mechanical royalties to a music publishing entity organized (and often wholly owned) by the singer/songwriter.

The third situation which occurred at the same time involved writers who were able, by reason of their contracts, to recapture their copyrights. They would designate a music publisher to administer the copyrights for the writer's own publishing company and receive the royalties. In that case however, the administering music publisher would no longer be receiving the "standard 50%" but would be receiving an administration fee of between 10% and 15% of the royalties paid by the record companies (including performing rights proceeds). Such administration agreements would endure for a limited period of time (i.e. three to five years) rather from the full term of copyright.

B. Do songwriters own the copyright or do music publishers?

I think that I have answered this question fully under part A.

C. What kind of fee does a songwriter get when a song is released as a record?

The rate payable to the copyright proprietor (see paragaraph A above) is a maximum royalty set by Section 115 of the 1976 Copyright Law. As of January 1986, that rate will be increased to 5¢ per single recording or .95¢ per minute of playing time, whichever is the larger. That is the maximum royalty that a record company is required to pay. The royalty is paid by the record company to the copyright proprietor (see paragraph A above). The share payable to the composer and lyricist has been discussed under part A.

D. Assuming his proposal passes, and I buy a blank cassette, which now sells for $2.10,for $3.00 where would the 90¢ go?

It would be divided among the copyright owners (i.e. the record company as the owner of the copyright on the recording and the parties who control the copyright to the music and lyrics.) Each of those groups would then subdivide the share of royalties allocated to their class to the people with whom they contract. In the case of the songwriter, see paragraph A above.

Question 2

Music publishers typically required unestablished songwriters to give up half of their royalties up front for the music publishers' service. Would these music publishers continue to get the benefit of this tax even for old popular songs which are basically selling themselves and do not require any help from music publishers?

The answer is covered by paragraph A, where we have stated "the royalty follows the copyright." When you use the term "half of their royalties" we assume that the Senator means that the composer/lyricist, as the initial copyright proprietor,is entitled to receive 100% of the royalties and that under the terms of the so-called "standard" contract, 50% are allocated to the music publisher. Further as stated in paragraph A the 50% is a "standard industry practice" which applies to all songwriters and not limited to merely novice songwriters.

Mr. GORTIKOV. Our next witness is one of the most prestigious economists: Dr. Alan Greenspan.

Senator MATHIAS. Dr. Greenspan, it is a pleasure to have you back with us. We will be happy to hear from you today.

STATEMENT OF ALAN GREENSPAN

Dr. GREENSPAN. Thank you very much, Mr. Chairman, Senator. I appreciate the opportunity to support S. 1739.

Although to some form of audio taping of records have been in use for years, the home taping emerged in the decade of the 1970's, particularly late in the decade, as a major factor affecting the music industry. In 1969 approximately one-fourth of U.S. households had home recording equipment. By 1977, 40 percent of U.S. households had home recording equipment. The most recent data suggests that more than three-fifths of households own 91 million audio taping units, and that new purchases are running at approximately 25 million units or more a year.

The cost of home taping is only 25 percent of the equivalent price of the recording at retail. Unless this gap narrows dramatically, we can expect that the share of the total market of recorded music accounted for by home taping will continue to rise.

Indeed, this trend is already ominous. Home taping has been rising at a very substantial pace in recent years. Assuming only a single use of a blank tape in 1972, home taping accounted for 20 percent of the total hours of recorded music available both from purchase and tape.

By 1984 home taping had risen to 40 percent of the total. The growing amount of home taping has had a substantial impact in displacing sales of prerecorded music. Sample data suggests that more than two-fifths of all home taping was in lieu of the purchase of prerecorded records or tapes last year. This represents lost sales of approximately 26 percent of the total volume of record sales in 1984.

When that loss is combined with the sales displaced by taping onto tapes previously used to record music or speech, and with the effect of taping on record prices, retail dollar losses from home taping last year amounted to about $1.5 billion. These losses were suffered by the music industry at a time when its profits remained depressed. The profit margins dropped sharply in 1979, but the industry probably as a whole is operating at a loss. The industry continued to experience losses in 1981 and 1982, and apparently barely broke even in 1983. Profits increased moderately in 1984 along with sales, but margins continued subdued or below what they were prior to the acceleration of home taping late in the 1970's. In fact, the recovery in margins is close to what one would have assumed granted the expansion of home taping. Thus, the impact of home taping on the industry is as evident today as it was in the industry's worst period in the early 1980's. The volume of sales lost through home taping has disturbing implications for the recording industry, as ultimately for those who purchase records. Already total releases are down the last 6 years by nearly one-half. It is obvious that as home taping continues to grow there will be fewer and fewer original performances on records for tapers to copy.

Clearly, for home taping to exist, there must be a record industry. Hence, it would be an extraordinary irony if the new, huge technological success of home taping led to its own demise. There are no winners in this process, but the recording industry supports a vast network of composers and performing artists and is the source of a very substantial proportion of radio programming. There is little that record companies can do to combat these losses. If the recording industry attempted to raise prices in an effort to recoup losses, it would only further reduce the sales of prerecorded music and probably increase the shift toward lower cost home taping.

If, alternatively, the record companies cut prices to narrow the gap between home taping costs and retail record prices, they would accelerate the profit deterioration in the industry and decrease their capability to take the type of risks that the nature of the recording business requires. Something meaningful must be done to right the severe economic damage caused by home taping.

My analysis indicates that the net loss actually sustained by the music industry, deducting those costs not incurred as a result of home taping, is nearly two-fifths of the $1.5 billion it is losing annually in sales and retail, or some $600 million. The royalties proposed in S. 1739 would apparently yield about $200 million annually, about one-third of what I estimate the actual loss is.

Even this solution, therefore, would fall short of the sum that should be compensable to copyright owners and creators. The Home Audio Recording Act is nonetheless an important step forward and represents a reasonable and creative response to the problems posed by home taping.

Thank you.

[Dr. Greenspan's submissions for the record follow:]

SUMMARY STATEMENT OF DR. ALAN GREENSPAN

SUBCOMMITTEE ON PATENTS, COPYRIGHTS AND TRADEMARKS
SENATE COMMITTEE ON THE JUDICIARY
OCTOBER 30, 1985

Home taping has caused, and will continue to cause, severe economic damage to the recording industry. The economic realities of home taping suggest that there is little that the industry can do to sustain its profitability in the face of continued widespread home taping. These conclusions are based on the following essential facts:

1. Home taping has been rising at a very substantial pace in recent years. Assuming only a single use of a blank tape, in 1972 home taping accounted for 20 percent of the total hours of recorded music available both from purchase and taping. By 1984 home taping had risen to 40 percent of the total.

2. This amount of home taping has had a substantial impact in displacing sales of sound recordings. Overall, more than two-fifths of all home taping was in lieu of the purchase of prerecorded records or tapes last year. This means that displaced sales resulting from home taping were equivalent to 26 percent of total record sales. When that loss is combined with the sales displaced by taping onto tapes that were being re-used and with the effect of taping on record prices, the estimated retail dollar loss from home taping last year amounted to about $1.5 billion.

3. Record company profit margins dropped sharply in 1979 with the industry as a whole probably operating at a loss. The industry continued to experience losses in 1981 and 1982, and apparently broke even in 1983. Profits increased moderately in 1984 along with sales, but margins continued subdued, far below what they were prior to the acceleration of home taping late in the 1970s. The impact of home taping on the industry is as evident today as it was in the industry's worst period in the early 1980s.

4. The volume of sales lost through home taping has disturbing implications for the recording industry and ultimately for those who purchase records. Already, total releases are down in the last six years by nearly one-half and employment in the industry has fallen off from its high of 29,000 in the late 1970s to 19,000 in 1984. It is obvious that, as home taping continues to grow, there will be fewer and fewer original performances on records for purchasers to enjoy and for tapers to copy.

5. If taping continues to erode record sales and profits, the recording industry might be forced to attempt to raise prices in an endeavor to recoup losses. That, however, would only further reduce the sales of prerecorded music and probably further increase the shift toward lower cost home taping.

6. Alternatively, the record companies might be pressured competitively to cut prices to narrow the gap between home taping costs and retail record prices. That, of course, woudl accelerate the profit deterioration in the industry and decrease its capability to take the types of risks which the nature of the record business requires.

7. The net loss actually sustained by the music industry is nearly two-fifths of the $1.5 billion it is losing annually in sales. Approximately $200 million would be yielded by the royalty rates in S. 1739, far short of the sum that should be compensable to copyright owners and creators.

STATEMENT OF ALAN GREENSPAN

RE: S. 1739

BEFORE THE SUBCOMMITTEE ON PATENTS,
COPYRIGHTS AND TRADEMARKS
SENATE COMMITTEE ON THE JUDICIARY

OCTOBER 30, 1985

Mr. Chairman, for the last several years, Townsend-Greenspan has been retained by the Recording Industry Association of America to provide an economic analysis of home audio taping of copyrighted sound recordings.[1] Our most recent analysis confirms our previous judgments relative to the damage that home taping has inflicted on the recording industry.

The basic purpose of our ongoing studies has been to estimate the impact and implications of home audio taping on unit sales and prices of discs and prerecorded tapes, and ultimately, on the ability of the recording industry to continue to meet the needs of the consumer public. That a large, and increasing, amount of home taping has been taking place is clearly evident, given the expansion in the sales of tape recorders and blank tapes. A key question, however, is what has been the impact of this activity on sales of prerecorded music? How, in effect, would the recording industry have evolved in recent years had home taping never technologically developed?

We have analyzed this question with the assistance of two basic sets of data: (1) the substantial amount of sample survey information on home taping practices from which inferences with respect to the impact on sales of recordings can be made, and (2) government and financial data on the markets for sound recordings, tape recorders and blank tapes. Both sets of data reflect the strong underlying growth in home audio taping and its negative impact on sales of prerecorded tapes and discs.

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[1] Dr. Greenspan is Chairman and President of Townsend-Greenspan & Co., Inc. of New York City.

Although some forms of audio taping of records have been in use for years, home taping emerged in the decade of the 1970s, particularly late in the decade, as a major factor affecting the music industry. In 1969, we estimate that approximately one-fourth of U.S. households had home recording equipment; by 1977 that figure had grown, with 40 percent of households reporting ownership. The most recent data suggest that more than three-fifths of American households own 91 million audio taping units and that new purchases are running at approximately 25 million to 28 million units a year.

From an economist's viewpoint, home taping should be viewed as an alternate means of acquiring recorded music. The price of acquiring music in the form of a record or prerecorded tape must, therefore, be compared with the cost of acquiring that music by taping it at home. The cost to a consumer of a prerecorded disc or tape is the retail purchase price. In contrast, it is more complex to identify the costs involved in the "purchase" of music through home taping. It consists of both the fixed costs of recording equipment and the out-of-pocket costs of blank tape.

Clearly, the cost of the recording equipment is in many cases a significant factor, and probably the most substantial potential barrier to the growth of taping. But once the fixed cost of the equipment has been paid and the equipment is in place, the costs of taping music become out-of-pocket only -- the cost of the blank tape. As indicated above, the data on audio recording equipment suggest that these fixed costs are no longer the barrier they once were -- given that approximately three-fifths of American households already own taping equipment, and there are annual additional purchases in excess of 25 million units a year.

The identification of the costs involved in the "purchase" of recorded music through home taping entails the appropriate allocation of both the cost of equipment and the cost of blank tape. We have estimated that the amortized 1984 cost of taping equipment is the equivalent of 48 cents per prerecorded disc or tape and that the cost of the blank tape in album equivalent terms was $1.19. Hence, the total "taping" costs, $1.67, were 25 percent of the equivalent 1984 price of the recording at retail, i.e., $6.80. Unless this gap narrows dramatically, we can expect that the share of the total market of recorded music accounted for by home taping will continue to rise. Obviously, the most significant part of this difference (perhaps all) reflects the failure -- in technical terms -- to amortize the capital costs reflected in the copyright. This means that tape and equipment manufacturers, and consumers who tape, can freely secure the benefits of the property rights of the copyright creators -- a matter of significant benefit to the former without any compensation whatsoever to the latter.

As one might expect, home taping has been rising at a very substantial pace in recent years. Assuming only a single use of a blank tape, in 1972 home taping accounted for 20 percent of the total hours of recorded music available both from purchase and taping. (This excludes music available from multiple uses of blank tapes, counterfeiting, and piracy.) By 1984, it had risen to 40 percent.

Sample data indicate that approximately three-fourths of the initial uses of newly acquired blank tape are to record music. Of that, approximately three-fifths of music taping is currently from owned or borrowed records and tapes. The remainder is used primarily to tape recordings from radio, TV or live performances. The next step -- determining the extent to which home taping displaces purchases of prerecorded records and tapes -- is complex. But it is clear that the number is substantial. From the available data, it appears that roughly half of the taping from borrowed records or tapes would have generated record or tape purchases had home audio taping not been possible. The data indicate that approximately 42 percent of the taping from owned records (mainly for car or office copies) would have resulted in purchases of additional records and prerecorded tapes. And, two-fifths of all the off-the-air taping probably would have generated record or tape purchases.

Overall, this suggests that more than two-fifths of home taping was in lieu of the purchase of prerecorded records or tapes last year. This represents lost sales of approximately 26 percent of the total volume of record sales in 1984.

This percentage of sales displaced by home taping is the equivalent in 1984 to lost record sales of more than $1 billion. In addition, sales are being displaced by taping over previously recorded music or speech. As home inventories of recorded tapes grow, this will become an increasing source of retail sales displacement. It is difficult to estimate the size of this displacement owing to the multiple use of tapes, but it could easily have amounted to more than a couple of hundred million dollars in 1984. Finally, we estimate that this sales displacement depressed prices on all record sales by at least five percent ($200 million) below what they otherwise would have been. Hence, we estimate the overall retail dollar losses from home taping last year were about $1.5 billion.

It should not be surprising to find an effect on the prices of recordings from home audio taping which displaces a significant amount of unit sales. Indeed, there is considerable evidence to suggest that the average price level for prerecorded tapes and discs last year, and presumably currently, was at least several percentage points lower than would have prevailed in a market not suppressed by home audio taping. Data from the CBS Consumer Panel show that prices of prerecorded tapes paralleled the average price level for all consumer goods and services from 1974-1978. From 1978-1984, however, average annual prices of prerecorded tapes went up 2.2 percent; the price of all consumer goods and services rose 6.7 percent per year on average. Had average prerecorded tape prices paralleled the general rise in consumer prices in 1984, they would have been 29 percent higher than they in fact turned out to be. It is apparent from the price structure patterns of recent years that the relative softness of record prices is not a response to lowered cost pressures, technological breakthroughs or some other industry-related factors.

On the contrary, the evidence suggests that the failure of the record price levels to rise in line with consumer prices generally was at the expense of profits, that is, a market-related inability to pass on increased costs. Profit margins dropped sharply in 1979, with the industry as a whole probably operating at a loss. The industry continued to experience losses in 1981 and 1982, and apparently barely broke even in 1983. Profits increased moderately in 1984 along with sales, but margins continued subdued, far below what they were prior to the acceleration of home taping late in the 1970s. In fact, the recovery in margins is close to what one would have assumed granted the expansion of home taping. Thus, the impact of home taping on the industry is as evident today as it was in the industry's worst period in the early 1980s.

We have reconstructed the industry's income statement on the assumption that the loss at retail of approximately $1.5 billion did not occur. Making what I would deem reasonable assumptions with respect to fixed and variable costs yields pretax profit margins only modestly above those which prevailed in the mid- to late-1970s. Hence, home taping would have been expected to reduce profit margins in a year such as 1984 to about where they eventually ended up. Given the state of consumer incomes and employment in 1984, some improvement in the record industry was to be assumed even after adjustment for the damaging effects of home taping. Thus, to point to the modest recovery as evidence of an easing of the taping problem is inappropriate.

The volume of lost sales through home taping, in light of this economic experience, poses disturbing implications for the recording industry and ultimately, for those who purchase records. Already, employment in the industry has fallen off from its high of 29,000 in the late 1970s to less than 19,000 in 1984. Total releases are down in the last six years by nearly one-half. It is obvious that, as home taping continues to grow, the sale of records produced by the recording industry will decline further. There will be fewer and fewer original performances on records for purchasers to enjoy and for tapers to copy. Clearly, for home taping to exist, there must be a record industry. Hence, it would be an extraordinary irony if the huge technological success of home taping led to its own demise. There are no winners in this process, for the recording industry supports a vast network of composers and performing artists, and is the source of a very significant proportion of radio programming.

There appears to be no successful pricing strategy for the industry to respond to the home taping problem. If taping continues to erode record sales and profits, the recording industry might be forced to attempt to raise prices in an endeavor to recoup losses. That, however, would only further reduce the sales of prerecorded music and probably increase the shift toward lower cost home taping.

Alternatively, record companies might be pressured competitively to cut prices to narrow the gap between home taping costs and retail record prices. That, of course, would accelerate the profit deterioration in the industry because costs are rigid; it would decrease the industry's capacity to take the types of risks which the nature of the record business requires.

Thus, there is very little that the recording industry can do to achieve sustained profitability in the face of the continued expansion of home taping. This is the case, notwithstanding what some observers see as sales opportunities from such advances as the compact disc. Any sales impetus would be only a temporary reprieve from economic pressures. They cannot avoid the drain on the industry from the competitive use of home audio taping.

For economic incentives to work appropriately, property rights must protect the rights of capital assets whether in physical or intangible form. At present, as the data show, home taping is causing severe economic damage to the property rights of owners of copyrights in sound recordings and musical compositions. Under present and emerging conditions, the industry simply has no out. Unless something meaningful is done to respond to the home taping problem, the industry itself is at risk.

While home taping may account for over $1.5 billion in lost sales to the music industry each year, it is obvious that not all of that sum represents actual losses to copyright owners and creators. For example, record companies do not incur the costs of manufacturing or distributing the records and prerecorded tapes whose sales are displaced by home taping. Accordingly, the compensation properly due copyright owners and creators is something less than the full value of their lost sales.

To estimate how much of the industry's losses should be compensable, I relied on the hypothetical income statement for the industry described earlier. This analysis revealed the incremental royalties and income that would have been earned by recording artists, composers, publishers, musicians' and performers' unions, and recording companies, or, stated otherwise, the net loss actually sustained by the music industry as a result of home taping.

My preliminary analysis of that income statement suggests that nearly two-fifths of the industry's retail losses should be compensable to copyright owners and creators.

I estimate that the royalty rates established by S. 1739 would yield approximately $200 million. (See Tables 8 and 9.) Although this amount falls far short of the sum that I believe should be compensable to copyright owners and creators, the Home Audio Recording Act is an important step forward. I commend this legislation to you as a reasonable and creative response to the problems posed by the technology of home taping.

TABLE 1

GROWTH IN HOME AUDIO TAPE RECORDING

	TAPE RECORDERS				BLANK TAPES (3)		
	Number of Units		Households Owning One or More Recorders (2)		Units Shipped		Playing Time Per Tape Recorder Unit in Use
	Shipped	in Use (1)(2)	Percent of all Households	Number	Number	Playing Time (4)	
	(Millions)			(Millions)	(Millions)	(Millions of Hours)	(Hours)
1969	6.93	20.74	26.3	16.60	122	71.1	3.4
1970	8.45	25.09	30.2	19.51	132	76.8	3.1
1971	8.75	28.87	32.8	21.84	142	82.7	2.9
1972	10.27	33.32	34.8	23.82	152	97.2	2.9
1973	10.78	37.41	37.0	25.99	163	113.1	3.0
1974	9.30	39.15	37.4	26.82	174	130.8	3.3
1975	7.82	38.77	36.0	26.45	192	157.6	4.1
1976	12.75	42.84	38.0	28.53	218	194.8	4.5
1977	13.68	47.21	40.2	30.93	234	225.7	4.8
1978	16.20	53.23	43.7	34.32	252	261.2	4.9
1979	16.30	58.30	46.0	37.01	226	250.0	4.3
1980	19.71	65.53	50.1	41.14	236	278.3	4.2
1981	22.57	74.39	55.4	46.20	238	298.0	4.0
1982	20.33	79.51	58.2	48.78	244	305.3	3.8
1983	21.44	84.35	60.1	51.12	256	320.0	3.8
1984	25.00	91.29	63.2	54.67	264	330.0	3.6

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(1) Shipments in each year were assumed to be scrapped according to the following schedule: current year, 2%; second year, 10%; third year, 15%; fourth year, 15%; fifth year, 15%; sixth year, 10%; seventh year, 10%; eighth year, 10%; ninth year, 8% tenth year, 5%.

(2) End of year.

(3) Cassette tapes and 8-track cartridges.

(4) All purposes.

Sources: U.S. Department of Commerce; "Merchandising," March 1983, March 1982, March 1981, March 1980; WCI; EIA; Townsend-Greenspan & Co.

TABLE 2

ILLUSTRATIVE COSTS INVOLVED IN
HOME TAPING OF RECORDED MUSIC IN 1984

A. Taping Equipment

1. Average cost of equipment: $34.07

   Allocate 1/2 of the cost for taping
   Assume a 5-year life
   Allocate 3.8 tapes per year per tape recorder

2. Cost of taping per cassette:

   $\$34.07 \div 2 \div 5 \div 3.8 = \$0.90$

3. Album equivalents per blank cassette (assume average 75 minutes per blank cassette)

   $$\frac{\text{Average playing time per blank cassette (75 minutes)}}{\text{Average album playing time (40 minutes)}} = 1.875$$

4. Cost of taping an album:

   $\$0.90 \div 1.875 =$ approximately 48¢

B. Blank Tape

1. Average cost per cassette (75 minute average): $2.24

2. Cost of a cassette in album equivalent terms:

   $\$2.24 \div 1.875 =$ approximately $1.19

C. Total Cost (in album equivalent terms)

1. Taping equipment	$ .48
2. Blank tape	1.19
3. Total	$1.67

Sources: Merchandising, March 1985; Townsend-Greenspan & Co.

TABLE 3

HOME TAPED PORTION OF TOTAL MUSIC HOURS (millions of hours)

From Blank Tapes					Pre-Recorded Music						All Sources	
1 Date	2 8-Track	3 Cassettes	4 Total	5 Music	6 Singles	7 Albums	8 8-Track	9 Cassettes	10 CDs	11 Total	13 Total Recorded Music	14 % From Blank Tape
1969	7.4	63.7	71.1	53.3	18.2	170.1	38.7	12.2		239.2	292.5	18.2%
1970	8.5	68.3	76.8	57.6	18.8	176.1	49.8	11.1		255.8	313.4	18.4%
1971	9.8	72.9	82.7	62.0	20.7	187.2	52.5	14.3		274.7	336.7	18.4%
1972	12.3	84.8	97.1	72.8	26.2	192.4	63.2	17.1		298.9	371.7	19.6%
1973	15.4	97.7	113.1	84.8	28.9	175.0	60.7	10.0		274.6	359.4	23.6%
1974	19.2	111 6	130.8	98.1	26.5	173.4	64.5	10.2		274.6	372.7	26.3%
1975	24.4	133 2	157.6	118.2	21.6	161.9	63.1	10.8		257.4	375.6	31.5%
1976	28.2	166 6	194.8	146.1	25.7	172.9	70.7	14.5		283.8	429.9	34.0%
1977	32.7	193 0	225.7	169.3	26.3	219.0	84.9	24.6		354.8	524.1	32.3%
1978	33.2	228 1	261.3	196.0	26.6	217.9	89.1	40.9		374.5	570.5	34.4%
1979	23.9	226.1	250.0	187.5	28.0	204.2	69.8	55.2		357.2	544.7	34.4%
1980	20.3	258 2	278.5	208.9	23.0	207.1	57.6	73.5		361.2	570.1	36.6%
1981	12.8	285 2	298.0	223.5	21.7	189.4	32.3	91.3		334.7	558.2	40.0%
1982	9.8	295.4	305.2	228.9	19.2	155.0	9.1	122.1		305.4	534.3	42.8%
1983	5.5	315.0	320.5	240.4	17.5	134.5	4.0	157.9	0.5	314.4	554.8	43.3%
1984	3.8	326.3	330.1	247.5	18.4	131.3	3.9	221.3	3.7	378.6	626.1	39.5%

Notes:

1. Average playing time x number of units shipped.

2. Includes speech, music and other.

Sources: RIAA, Merchandising Magazine, March 1985, March 1983, March 1982, March 1981, March 1980; Billboard Magazine, August 26, 1972, Townsend-Greenspan & Co.

TABLE 4

PROPORTION OF HOME TAPING DISPLACING PURCHASES OF PRE-RECORDED MUSIC

Source of Taping	Percent Taping	Percent Who Would Have Purchased if Taping Unavailable
From owned or borrowed records or tapes	60.8%	44.1%
From radio, TV or live performance	39.2	40.2
Totals	100.0%	42.6%

Note: The 42.6% was calculated using the percent taping as weights.

Sources: Audits and Surveys; Townsend-Greenspan & Co.

TABLE 5

ESTIMATED MARKET VOLUME[1]
DISPLACED BY HOME TAPING IN 1984

Method I

(1)	Blank tape purchases (in units)	263.9 million	(Merchandising)
(2)	Seventy-five percent used for music taping	197.9 million	(1) x .75
(3)	Percent displacing retail purchases	42.6%	(Table 4)
(4)	Number displacing retail purchases	84.3 million	(2) x (3)
(5)	Album equivalents	158.1 million	(1.875 x (4))
(6)	Displaced purchases, realized market value	$1,075.1 million	((5) x $6.80 per album)

Method II

(1)	Music hours recorded on blank tape	247.5 million	(Table 3)
(2)	Percent displacing retail purchases	42.6%	(Table 4)
(3)	Displaced retail purchases (in hours)	105.4 million	(1) x (2)
(4)	Retail sales of music recordings (in hours)	378.6 million	(Table 3)
(5)	Displaced purchases as percent of actual retail	27.8%	(3) ÷ (4)
(6)	Retail sales of music recordings	$3,907 million	
(7)	Displaced purchases, realized market value	$1,086.2 million	(5) x (6)

[1] Assuming a single use of a blank tape bought in 1984.

Source: Townsend-Greenspan & Co.

TABLE 6

RETAIL PRE-RECORDED TAPE PRICES COMPARED WITH AVERAGE CONSUMER PRICES

	Average Price Paid for a Pre-Recorded Tape	Price Level for All Consumer Goods and Services	Retail Price Ratio of Pre-Recorded Tape to All Consumer Goods and Services
	(Dollars)	(1972 = 100)	
1974	$4.69	116.3	.0403
1975	4.99	125.1	.0399
1976	5.26	131.7	.0399
1977	5.55	139.3	.0398
1978	5.96	149.0	.0400
1979	6.12	162.5	.0377
1980	6.48	179.0	.0362
1981	6.56	194.6	.0337
1982	6.72	206.0	.0326
1983	6.80	213.6	.0318
1984	6.80	220.4	.0309

Sources: CRU Consumer Panel; U.S. Department of Commerce

TABLE 7

EMPLOYMENT DATA

THE SOUND RECORDING INDUSTRY

Annual	Employment (thousands)
1972	25.0
1973	24.8
1974	23.7
1975	22.1
1976	25.2
1977	26.5
1978	28.7
1979	27.2
1980	24.6
1981	24.8
1982	20.5
1983	19.4
1984	18.8

Source: U.S. Bureau of Labor Statistics

TABLE 8

ESTIMATED YIELD OF BLANK TAPE ROYALTY

1(a) Tape Type	2 Length (Minutes)	3 % of Total Sales (units)	4(b) Unit Sales (000)	5 Total Minutes (000) (2*4)	6 Royalty Rate Per Minute	7 Royalty Yield (000)
Premium						
	46	5%	7,177.50	330,165.00	$0.01	$ 3,301.65
	60	15%	21,532.50	1,291,950.00		12,919.50
	90	80%	114,840.00	10,335,600.00		103,356.00
Total		100%	143,550.00	11,957,715.00		$119,577.15
(Exempt Tapes)(c)		11%	(15,790.50)	(1,315,348.65)		($13,153.49)
NET TOTAL			127,759.50	10,642,366.35		$106,423.66

Notes and Sources:

(a) Non-premium tapes have been excluded from this calculation on the ground that they are likely to be exempt from royalty fees under the Home Audio Recording Act.

(b) Total 1984 sales equal 261 million, per Merchandising Magazine, March, 1985, page 94. Premium tapes constitute 55% of total unit sales in 1984, per Mart Magazine, March, 1985, page 80.

(c) 11% of all cassettes purchased are for exempted purposes under the Home Audio Recording Act, such as school or office use. ("A Consumer Survey: Home Taping" by Warner Communications Inc., 1982, page 9.)

TABLE 9

Estimated Yield of Equipment Royalty

Equipment Type	1 Units(a) (000)	2 % Dual	3 # Single (000)	4 # Dual (000)	5 Total Retail Value (a) (000)	6 Total Wholesale Value(i)	7 Single Wholesale Value (6-8)	8 Dual Whole-sale Value (2-6)	9 Single Royalty 5%	10 Dual Royalty 25%	11 Total Royalty (000)
Components:											
Tape decks:											
Cassette	816.000	24.00%(e)	620.160	195.840	$138,084	$110,467	$ 83,955	$ 26,512	$ 4,198	$ 6,628	$10,826
8-Track	26.000	0.00%	26.000	0.000	19,968	15,974	15,974	0	799	0	799
Reel-to-reel	48.000	0.00%	48.000	0.000	3,236	2,589	2,589	0	129	0	129
Compact Systems:											
Cassette (b)	1330.000	18.30%(f)	1086.610	243.390	293,217	234,574	191,647	42,927	9,582	10,732	20,314
8-Track Recorder	352.000	0.00	352.000	0.000	45,759	36,607	36,607	0	1,830	0	1,830
Personal Portable:											
Cassette (c)	1219.000	0.00%	1219.000	0.000	96,301(h)	77,041	77,041	0	3,852	0	3,852
Radio/ Cassette (c)	967.000	0.00%	967.000	0.000	76,393(h)	61,114	61,114	0	3,056	0	3,056
Portable Tape Equipment:											
Cassette Recorders	12800.000	7.20%(g)	11878.400	921.600	436,096	348,877	323,758	25,119	16,188	6,280	22,468
8-Track Players/ Recorders	385.000	0.00%	385.000	0.000	15,843	12,674	12,674	0	634	0	634
Radio/ Cassette Combin. (d)	9,993.000	7.20%(g)	9,273.504	719.496	620,142	496,114	460,393	35,720	23,020	8,930	31,950
TOTALS	27,936.00		25,855.674	2,080.326	$1745,039	$1396,031	$1265,753	$130,278	$63,288	$32,570	$95,857

Notes on Table 9
Estimated Yield of Equipment Royalty

(a) Units shipped and retail values (except for retail values of personal portable cassette machines) listed in Merchandising Magazine, March 1985, page 88. These numbers differ somewhat from those in Table 1, owing to differing sources.

(b) Merchandising Magazine reports 1984 shipments of compact systems with cassettes at 1.829 million units. U.S. Department of Commerce reports that in 1983, 72.7% of all audio tape equipment imports, in units, were recorders/players (21.189 million) while 27.3% were players only (7.960 million).

Thus the total number of compact systems with cassette reported (by Merchandising Magazine) in 1984 has been multiplied by .727 to arrive at the approximate number of recorders.

(c) The EIA Consumer Electronics Annual Review, 1984, reports recent developments in pocket-sized stereos with headphones (also called "personal portables"). These combine miniaturization with top quality sound and may be purchased with radio only, cassette only, or a radio/cassette combination. "Like the standard cassette recorder, many headphone cassette systems also have recording capability."

The EIA Audio Industry Consumer Study, March 1985, page 58, reports that 34.1% of the people who bought personal portable stereos with cassette in 1984 purchased recording capability. Thus, the total number of shipped personal portables with cassette reported in 1984 (by Merchandising) 6,411 million, has been multiplied by .341 to arrive at the number of cassette recorders in this product category.

(d) Merchandising Magazine reports that 13,745 million units of portable radio/cassette players (distinct from personal portables with headphones) were shipped in 1984.

This has been multiplied by .727 (see (b) above) to arrive at the approximate number with recording capability.

(e) The EIA Audio Industry Consumer Study, page 31, reports that in 1984 9.4% of U.S. households had purchased cassette tape decks within the past two years: 7.2% had purchased single cassette tape decks and 2.3% had purchased dual cassette tape decks. Thus, approximately 76% (7.2 divided by 9.5) of cassette tape decks purchased between 1982 and 1984 were single cassette while approximately 24% were dual cassette.

(f) In 1984, according to the EIA Audio Industry Consumer Study, page 29, 18.3% of owners of a compact system with cassette said that theirs was a dual cassette system. Thus, the 1,330 compact cassette units shipped in 1984 has been multiplied by .183 to achieve an estimated number of dual cassette compact systems.

(g) According to the EIA Audio Industry Consumer Study, page 64, 7.2% of portable AM/FM Radio/Cassette combinations purchased in 1984 were dual cassette. The same percentage of portable cassette recorders without radio are here assumed to be dual.

(h) The retail value of personal portable cassette players was not reported by Merchandising Magazine in the 63rd Annual Statistical and Marketing Report. An informal survey conducted shows the average retail price of a personal portable cassette player (or cassette/radio combination) to be approximately $79.00. This unit price has been used to arrive at an estimated total retail value for this product category.

(i) Audio equipment margins at the retail level range from 15-35% according to a 1985 report by Arthur D. Little to the Electronic Industries Association/Consumer Electronic Group. (Consumer Electronics: A $40 Billion American Industry, pages 25-26.) Thus, in this analysis, a 25% retail margin has been assumed and retail values reported by Merchandising have been divided by 1.25 to reach an average wholesale value.

METHODOLOGY AND STATISTICAL APPENDIX

Industry, trade (1) and government sources provided data on shipments of sound recordings, blank tapes and audio tape recorder equipment. Sample surveys documented various aspects of home taping practices. Although, for any given year, shipments are not identical with consumer purchases, the trends and levels of both series were presumed to be roughly similar, and for this study shipments were used as an indicator of sales.

Estimating Taping Equipment Ownership

A historical series on the number of households in the United States as of the end of the year was derived from U.S. Census data. From the WCI studies, the percent of households with audio taping equipment was available for April, May 1977 and May, June 1980. These studies also indicated the proportion of households owning at least one 8-track, cassette, and reel-to-reel recorder and hence the sum of those percents indicated multiple ownership of different types, but not of the same type. EIA studies of ownership were also available for 1980, 1982 and 1984, giving music capable taping units, as well as some indication of average age of some of the taping equipment in place at the time of the survey. A historical series on the number of audio tape recorders shipped each year, both domestic and imports, was compiled from U.S. Department of Commerce data. For domestic shipments prior to 1973, the data were linked to EIA industry estimates. Combining recent ownership data with previous sales implied a survival pattern which is, of course, approximate.

To arrive at a series on the number of tape recorders in place at the end of the year, shipments in each year were assumed to be scrapped according to the following schedule: current year, 2 percent; second year, 10 percent; third year, 15 percent; fourth year, 15 percent; fifth year, 15 percent; sixth year, 10 percent; seventh year, 10 percent; eighth year, 10 percent; ninth year, 8 percent; tenth year, 5 percent. The next step was to estimate the number of households owning one or more audio tape recorders and the percent this was of all households. The average number of audio tape recorders per taper owning household implied from the WCI studies and estimates of units in use was 1.50 at the end of 1976 and 1.57 at the end of 1979. Considering the recent growth in the shipment of audio tape recorders, we concluded that the prevalence of multiple taper households was relatively small a decade ago. As a consequence, we assumed an average 1.25 audio tape recorders per taper owning household at the end of 1969 and obtained intervening years by interpolation. The series on the number of tape recorders in use and the average number of audio tape recorders owned by taper owning households yielded an annual series on the number of households owning one or more audio tape recorders.

Estimating Costs Involved in Home Taping

The costs involved in home taping include the cost of the equipment and the cost of the blank tape itself. For illustrative purposes, the approximate cost of a portable cassette tape recorder and a cassette tape were used. These were derived from statistical data on retail sales dollar volume and number of units shipped (including imports) as reported in the trade publication "Merchandising." Table 2 details the cost derivation.

Estimating the Hours of Recorded Music

Recorded music is available both from purchases and home taping. The first step in estimating total hours of recorded music available from purchases was to obtain a historical series on unit shipments by the recording industry. These data were available from RIAA from 1973 forward. For the period 1969-1972, unit shipments of 8-track cartridges and cassette tapes were estimated from available dollar volume and an estimate of unit price based on a sample of reporting companies. In the case of singles and albums, a similar procedure was used, employing the available dollar volume for total discs as a control.

The next step was to estimate playing time per sound recording unit. For 8-track cartridges and cassettes, this was assumed to be an average of 40 minutes in all years. For singles and albums, data on tune length and album length were available for the years 1965, 1973 and 1980. Intervening years were interpolated. Finally, total playing time (unit shipments x playing time per unit) was estimated separately for singles, albums, cartridges and cassettes, and summed to arrive at total hours of recorded music from purchases of sound recordings. The data can be found in Table 3.

A similar procedure was followed in estimating total hours of recorded music available from home taping. Data on unit shipments (including imports) of blank cartridges and cassettes were available from the trade publication "Merchandising," beginning in 1974. For cassettes, an available 1971 estimate by the trade publication "Billboard" of the number of units shipped allowed us to interpolate the missing years, 1972 and 1973.

Average playing time per blank tape was estimated at 35 minutes in 1971, since mostly C-30 and C-40 cassettes were in use at that time. Similarly, because C-60 and C-90 tapes were used most often in recent years, an average of 75 minutes of playing time per unit was used. Intervening years were estimated by interpolating.

The next step was to calculate total playing time available on blank tapes for all purposes by multiplying unit shipments by playing time per unit. The recent WCI study indicated that 75 percent of all blank tapes was used to record music, the remaining 25 percent being used to record speech in school or at the office and for personal or family recordings. Applying the 75 percent figure to total hours of playing time for all purposes provided a measure of total hours of recorded music available from home taping. The data can be found in Table 3.

Evaluating the Retail Dollar Losses from Home Taping

Home taping has impacted the sound recording industry by affecting sales and depressing prices. In order to evaluate the retail dollar losses, we first derived an estimate of the extent to which home taping displaced the purchase of prerecorded music using sample data. The derivation can be found in Table 4. We estimated that 42.6 percent of home taping was a substitute for purchase.

We have used two approaches to convert this percentage into retail dollar losses. The starting point of the first was the number of blank tapes purchased. The second approach used the number of music hours recorded on blank tape. Both methods yield a figure of approximately $1 billion and are detailed in Table 5.

To this figure we have added an estimate of the extent to which the displaced sales depressed prices. As can be seen from Table 6, the average price of prerecorded tapes tracked the implicit price index for all consumer expenditures fairly closely through 1978 but, beginning in 1979, tape prices lagged. By 1984 the divergence had cumulated to 29 percent. Data collected for the years 1974 through 1979 (2) indicate that gross profit margins were stable between 1974 through 1978, but dropped sharply in 1979 suggesting that the failure of tape prices to match consumer price increases in 1979 reflected competitive factors such as home taping. Unpublished sources for 1980-1984 indicate only a modest margin improvement, confirming the presumption of prices being depressed from the market, as distinct from the cost side. We have used "at least 5%" to provide a conservative estimate of how much of the retail dollar loss was attributable to depressed prices.

RESPONSES OF DR. ALAN GREENSPAN TO QUESTIONS SUBMITTED BY SENATORS MATHIAS AND DECONCINI

Dr. Alan Greenspan submits this response to written questions submitted by Senators Mathias and DeConcini on S. 1739, the Home Audio Recording Act.

I. QUESTIONS SUBMITTED BY SENATOR MATHIAS

Critics of S. 1739 have said that the royalty rates for machines and tapes are arbitrary and that they are unrelated to the harm inflicted by home taping. Are the royalty levels contained in this bill out of proportion to the losses suffered by the recording industry?

From a purely economic point of view, what royalty level would be adequate to compensate the recording industry for its losses due to unauthorized home taping?

In principle, the royalties on machines and tapes should fully restore the property rights of owners of copyrights in sound recordings and musical compositions, by compensating them for all of the losses they suffer as a result of home taping. The rates set in S. 1739, however, provide only partial compensation to copyright owners. This is because the proposed royalties will generate an amount that is less than the measurable losses resulting from home taping.

From a purely economic point of view, I estimate that the music industry is losing approximately $600 million annually as a result of home taping. As discussed in my testimony, this estimate is based on an analysis of a hypothetical income statement I constructed for the recording industry. That analysis revealed the incremental royalties and income that would have been earned by recording artists, composers, publishers, musicians' and performers' unions, and recording companies -- or, stated otherwise, the net loss actually sustained by the music industry as a result of home taping -- and suggested that nearly two-fifths of the industry's $1.5 billion retail losses should be compensable to copyright owners and creators.

I estimate, however, that the royalty rates proposed in S. 1739 will yield only about one third of that amount, or $200 million annually.

II. QUESTIONS SUBMITTED BY SENATOR DECONCINI

1. Isn't it true that Walkman, boom boxes, car stereos, and other innovative tape devices have made high fidelity music more portable and popular and consequently created an enormous new market for music purchases? Why then does your analysis ignore the benefits of these technologies?

My analysis does not ignore the benefit of new technologies. Records, like other consumer goods, are affected by new technology, and the opportunities afforded by that technology are part of the reason that the music industry has enjoyed modest gains in sales revenues since 1983. Those gains do not, however, erase the measurable losses caused by home taping; were it not for home taping, greater improvement in record sales could have been expected.

In any event, the gains experienced by -- and the economic health of -- the music industry are ultimately irrelevant to the fundamental principle underlying this legislation: that copyright owners and music creators have a legal as well as an equitable right to be paid for their intellectual property by those who tape copyrighted prerecorded music. The music industry is not requesting compensation for its home taping losses because the industry is doing poorly; the industry is seeking compensation because home tapers are displacing sales and are thus taking a valuable right from copyright owners without appropriate compensation. Compensation for this displacement is required regardless of any gains the industry may enjoy from other sources.

2. In 1982, consumers spent $8.9 billion on Pac Man and other video games. Since then revenues from these games dropped by over $4.5 billion. Do you agree that video games and records compete for the same dollars and that Pac Man's loss was the record industry's gain?

The shift of consumer dollars away from video games may well have affected retail sales of records, since video games and music offer competing alternatives for recreational expenditures. The interaction of record sales and expenditures on video games is, however, ultimately irrelevant to any analysis of the measurable damage that home taping has inflicted on the music industry. My analysis of the economic losses caused by home taping was independent of increases or decreases in record sales attributable to other causes; as that analysis demonstrated, moreover, even in 1984 -- a year in which expenditures for video games purportedly decreased -- home taping resulted in losses of $1.5 billion in sales revenues to the music industry. Copyright owners and creators should be compensated for these losses regardless of the industry's gains or losses from other sources.

3. Am I correct that your testimony today relies on the same analysis you presented to the committee in 1983? And, isn't the validity of that analysis undercut by your erroneous predictions of doom for the record industry and the great profits that industry is experiencing?

My current testimony updates the analysis I presented in 1983, and reinforces the conclusions I reached at that time: that home taping has caused and will continue to cause severe long term economic damage to the music industry. My 1983 analysis did not predict that home taping would immediately cause the demise of the music industry; rather, it pointed to the damage -- to employment in the industry, profit levels, and the continued production of music -- that could be expected to occur over time if unauthorized home taping were not redressed.

Nothing in the music industry's current situation undermines the validity of that analysis. Moreover, it is inaccurate to suggest that the industry is experiencing great profits; as noted in my testimony, profit margins remain depressed in large part as a reflection of the losses caused by home taping. In fact, any increase in profit margins is largely a function of the state of consumer incomes and employment in 1984, and not of an easing of the home taping problem. The impact of home taping on the industry is as evident today as it was in the industry's worst period in the early 1980s, and the implications for the music business, and for those who purchase records, remain as disturbing as they were in 1983.

Mr. **Gortikov**. Mr. Chairman, when we began this panel's testimony, we pushed a button on this dual cassette machine over to your right. In its two cavities were one blank cassette and one copyrighted prerecorded jazz cassette. After only 9¼ minutes, that complete album has been duplicated, and that is one reason why we are here before you.

Senator **Mathias**. Which machine?

Mr. **Gortikov**. The one on your right.

Senator **Mathias**. Do you want to identify the machine?

Mr. **Gortikov**. A Sony CFS W600.

Senator **Mathias**. Dr. Greenspan touched on one of the questions that I was going to ask, and that is that there is at least the aura of prosperity about the recording industry today. In spite of this taping, the figures you gave offset that impression that you are in a hardship area. I assume from your statement that you would conclude that the industry's prosperity is not so great that it can offset the impact of these technologies.

Dr. **Greenspan**. That is correct, Mr. Chairman. It is certainly true that the industry is doing better than it did in 1982, but then so are all consumer industries. In fact, when we track the record industry with respect to units, prices and profits, we observe the very pronounced evidence of expanding home taping.

Nonetheless, there is still a cycle in the recording industry in the sense that it did poorly, as did all consumer goods in the early 1980's. It did better in 1983 and 1984. There was a boom in the consumer markets.

The recording industry, however, did less well in the sense that the track of home taping losses is very clear, even as the industry recovers partially. Profitability, nonetheless, remains far below where it would have been, in my judgment, had home taping not existed.

Mr. GORTIKOV. What the presumed prosperity also masks is that while a couple of companies may be doing very well at one point in time, many companies are still in a loss position. As to performance this year, the first 6 months of this year, our unit sales are down more than 4 percent, dollar sales are about flat.

Senator MATHIAS. That encourages the general view, and encourages some of the testimony we may get later this morning. When you say some companies are in a loss position, would you say many are?

Mr. GORTIKOV. I would say of those that are surveyed, a majority.

Senator MATHIAS. More than half?

Mr. GORTIKOV. Yes.

Senator MATHIAS. Senator Metzenbaum has gone to answer a rollcall vote. I hope the staff will call that testimony to his attention.

I will have to go vote in just a minute. I will try to wait until Senator Metzenbaum gets back. I will propound one more question before I go.

One of the assumptions that we make in considering this legislation is that proceeds of the royalties will be used to help cultivate new talent and will be channeled into some of the less profitable musical forms; that it will not all go, as Senator Metzenbaum suggested, to the superstars who are already making extraordinarily large sums of money.

How does the industry currently allocate resources to new talents to less profitable forms of entertainment?

Mr. GORTIKOV. I will speak to the record company portion. Mr. Weiss can speak to the creator portions.

The record industry and record companies are fueled by new talent, and the development of new talent and new music forms. They must exist on that new music flow. The capacity of those companies to finance talent discovery and development must come from profit. If the profit is diminished by home taping, the capability of seeking out new talent has to be proportionately suppressed.

If more revenue can flow from the proposal in this legislation that will enhance the ability of a record company to maximize or optimize its investment in new music. Right now some music forms are literally subsidized, like most classical recordings are subsidized by the hit recordings. We are in a highly competitive business, a high-risk business. Five out of six recordings released do not recover their cost.

Mr. WEISS. You know, as far as I can remember, since the day I started, publishers and record companies have traditionally taken moneys generated from their successes to help new people. Beverly Sills put it very well when she said she thanks the Beatles for her career, because it was the profit that Capitol Records made on the Beatles' records that allowed them to underwrite her operatic recordings.

I doubt we would have ever heard of her had it not been for the Beatles. When I started, publishers put money into me. They made demos of my songs when I almost had not written my own name, and I have been forever grateful for that.

I doubt if I had not had those publishers if anything would have happened to my career. One of the things that I would like to say is that the present-day songwriters and artists who have been able to get their work done will certainly benefit from this, because they will get paid from the pool, but I must say one word for superstars and another word for America.

What is wrong with building a better mousetrap or making a better record and then getting paid for it if the people want it badly enough? Let them beat a path to your door, and I say if a superstar makes a better record that people want, I say more power to him. Why not? That is what America is all about. You do not go to Macy's or Gimbel's and Sears and say you have made *x* amount of money this year, so from now on you are going to give the rest of your merchandise away free for the rest of the year. We don't do that in America, and I do not think you should do that even to a superstar, much as I would wish I was one, and I am not, but this legislation helps the brandnew writer and singer, the present-day one who has got the hits now, and the superstars should not be told that because they are now successful they should not earn anymore.

Thank you.

Mr. GORTIKOV. Mr. Chairman, I said one out of every six recordings fails to recover its cost. Five out of six fail. One out of six is profitable.

Senator MATHIAS. One out of six?

Mr. GORTIKOV. Yes.

Senator MATHIAS. Senator Metzenbaum.

Senator METZENBAUM. I think you understand we have a rollcall on, and that is the reason we are rotating bases.

I understand that one of you testified that most record companies are losing money. Can you give me some evidentiary backup for that, tell me which ones they are and how much they have lost within approximate figures?

Mr. GORTIKOV. No, sir, I cannot. That information is confidential. Nor can I myself——[laughter].

Nor can I myself identify those companies. Profit information is communicated through a firm of certified public accountants, who then consolidate it on an industrywide basis. The statistics are not revealed, even to association executives, as to their individual origin, but the majority of companies that have communicated profit information to our certified public accounting firm, a majority of those were in a loss position for the 1984 period.

Senator METZENBAUM. I have some information that CBS Record Group had $109 million operating profit on $1,150 million of sales in 1983, and an all-time single company high of $123 million operating profit on $1,270 million of sales in 1984.

RCA recorded on its 1983 annual report that sales of audio records and cassettes increased and combined with strong cost controls resulted in significantly enhanced profits. That trend continued in 1984 with profits through the third quarter.

WCI Records Group also called 1984 the biggest year ever. In 1985, WCI Records Group posted its highest first-quarter revenues ever. Revenues from MCA's and Music Group, which includes some home video sales, jumped to $259 million from 1983 to a total of $188 million. With the industry coming before us and asking for legislation by reason of the statistics that you have offered, it seems to me that it is somewhat obligatory for someone in the industry to waive any confidentiality, since I cannot understand what special purpose is served in saying, well, we really do not want to tell the world we lost $50 million or $5 million last year.

Dr. **Greenspan**. Senator, if I may respond to that. I have seen not the individual company data, but a major accounting firm has collected data on approximately four-fifths of the industry and has a unified set of accounts for U.S. recording operations. I have seen the combined totals, and I can attest to the fact that the data do not support the phrases which you quote. The reasons are manyfold. The data in the annual reports and elsewhere combine nonrecord industries operations on occasion and often mix domestic and international considerations. I was quite surprised when I saw the actual unified set of data compiled by this accounting firm from the individual unpublished reports. I do agree with you in the sense that the data that they reported to the major accounting firm, which I have seen in considerable detail, does not sound like the quotes that you cite. I understand that occurring largely because of the way that annual reports are often written.

Senator **Metzenbaum**. Well, Mr. Greenspan, of all the people that I can think of who might be involved in this issue, I cannot think of anyone whose record and past history would not fully understand our position of wanting to deal with facts. You dealt with figures, and I guess as I sit here I say to myself as a former business person, what is so secretive about whether the company made or lost a certain amount of money? We have literally hundreds of companies, thousands of companies listed on the New York Stock Exchange, the American Stock Exchange, the over-the-counter market, who revealed their facts and figures regularly, without any harm.

We are not asking for proprietary information. I do not care whether you gave it to some certified public accountants. What difference does that make?

I want to know what the facts are for my decision, and since I cannot comprehend the reasons for not sharing the information with us, I tell you very candidly that I believe your case is substantially weakened without submitting the facts. And I would urge you to reconsider the industry position.

Mr. **Gortikov**. Senator, one fact you might want to factor into your decisionmaking is the reality that 325 million albums that are home taped each year, by the admission of the home tapers themselves, would have been bought. That is a deprivation to an industry.

Senator **Metzenbaum**. That is a part of the equation.

Mr. **Gortikov**. It must be considered.

Senator **Metzenbaum**. The other part of the equation must be whether the industry is hurting economically. You made that recommendation. You gave us some charts to suggest that at least by implication, and it seems to me, and I just tell you, and I really do not care much whether you do or you do not, but I will say to you that I think that I and other members of the U.S. Senate would think that the industry's position is somewhat weakened by the failure to share the facts with us, particularly when we do not know why the facts are not shared. If we are asking for some proprietary information——

Mr. GORTIKOV. I respectfully urge you not to lose sight of why we are here. Two industries are being built and are making profits on the works of the constituencies we represent, and those are the ones that we are asking to share in this.

Also, when the industry was publicized as being in its lowest doldrums, the position of our opposition was exactly the same. They were equally opposed to any compensation.

So their position is the same. Whether or not we make money or lose money, it is the same. They want a free lunch. They do not want to pay anything. So that reality must not be evaded, as we look at the facts.

Senator METZENBAUM. I do not intend to evade anything, Mr. Gortikov.

Is there any other product or service that you know about that requires consumers to pay such a tax?

Mr. GORTIKOV. Well, the bill provides no tax whatsoever. A tax goes to the Government and is retained by the Government. This is not a tax. This is a royalty. I also do not know of any other commodity in which an individual can acquire a replication for free. If you want two copies of the Washington Post, you pay for them. If you want two copies of a book, you pay for them. If you want two cans of coffee, you pay for them.

Why, then, should two records be available while paying for only one?

Senator METZENBAUM. Cannot I make a copy of the Washington Post without paying for it?

Mr. GORTIKOV. You will be infringing on their copyright.

Senator METZENBAUM. If it is copyrighted.

Mr. GORTIKOV. If it is practical for you to do that.

Senator METZENBAUM. How do you anticipate how the royalties will be divided? What guarantees are there that the record companies and the performers who are already making millions of dollars will not get most of the money?

Mr. GORTIKOV. Well, the last part of your thesis is not exactly true.

Senator METZENBAUM. I have no way of knowing. You do.

Mr. GORTIKOV. The bill provides for regulations to be set up that would deal with the royalty sharing. The constituencies that are potential recipients are in agreement with the general principle of sharing—composers, publishers representatives of the two music-related unions, and the recording companies. It would be up to a government agency to decide regulations that would govern the sharing. The bill provides that it would basically track home taping that occurs from airplay and from home taping of records that are sold, and either of those can be used as guidance to the fair sharing.

Mr. WEISS. The premise of our business that I am aware of is to each according to his own contribution. We have those bases in place that have efficiently done this, know how to do it, and have done it honestly.

Incidentally, under government aegis, ASCAP is under government scrutiny, and there is no doubt in my mind that if somebody writes a song that sold 1,000 copies, he will stand as good a chance of getting it as somebody like Michael Jackson, who sold 5 million.

As I said before, there is nothing wrong with Michael Jackson getting paid for 6 million if he sold 6 million. Why should we tell him at 5 million to stop getting paid.

Senator METZENBAUM. Do you think, Mr. Weiss, it is possible that certain recordings, maybe classical recordings, might be copied more than certain other kinds or vice versa?

Mr. WEISS. I could not indulge in conjecture.

Senator METZENBAUM. The area about which you are speaking, there is a way of monitoring the number of times that a particular record is played, because it goes out over the airwaves. There is no way of recording how many home copies are made. That might be 10 times as many in one area, or one-fifth as much in another area, and so the bill provides that all such claimants shall negotiate in good faith among themselves in an effort to agree to a voluntary proposal for the distribution of royalty fees. That is nice language, but how does it get resolved, and how do we in the Congress legislate to that effect?

Mr. WEISS. I think just the way it was said. Of course, these people will negotiate just how it is set up now. They do it now to the best of their ability, up to 90 and 95 percent accuracy. They have monitored and reported as to what has been played and sold, and I think we can use those data bases to do the same thing here. There are some people who unfortunately slip through the cracks and do not get an exact count. That is what happens in many of our businesses, and it does not mean that an entire industry should be penalized and we should not get what is due us for our copyrighted material because of the accident of a few people not being able to get caught for what they have had performed. Not "caught." Monitored. Not "caught," judicially speaking, but in the parlance of the entertainment industry.

Senator METZENBAUM. The bill creates an antitrust exemption for copyright holders to get together to split up the revenue. Why should there be an antitrust exemption? If there are no competitive problems, there will not be any liability under the antitrust laws, but if there are antitrust problems, why create an exemption?

Mr. GORTIKOV. I would rather get you a lawyer's view of that. I am not a lawyer. I do know one thing. It does not directly respond to your question, but there is a reality in that there is a technical solution to all this that is available. It requires the cooperation of the equipment makers, and, therefore, it seems unachieveable, but it is entirely possible technologically to embed within a sound recording today a subliminal signal which would require in the taping equipment a compatible chip. That would mean that copyrighted recordings could be protected from infringement and home copying; whereas, noncopyrighted works—political speeches, and other items—could readily be taped and fully accessible to the taping process by the home taper. This would require the cooperation and willingness of the equipment manufacturers, and probably, therefore, require legislation to make it mandatory. But there is a fair, equitable technological solution available that would protect copyright owners and, as well, permit full access to noninfringing uses.

Senator **Metzenbaum**. I just want to share with the chairman and the other coauthors of this bill that there seems to be a real difference in factual presentation as to whether the recording companies are or are not doing well in the economy. There is some evidence to indicate that their profits are up. Mr. Gortikov says that their profits are down, but the figures are not available to us. I have asked why they are not available. He says they are submitted to certified public accountants and that the combined figures have been—he has seen those, and Mr. Greenspan says the same. They are down.

My view is that we ought to have the facts, and absent the fact that some of us who are concerned about some of that legislation have not made up our minds certainly can find dealing with those issues more difficult. Mr. Gortikov responded that that is not the issue, that the issue has to do with the idea of pirating——

Mr. **Gortikov**. Sir, my lawyer has passed me a brief note responding to your question about the antitrust exemption. The antitrust exemption in the bill follows the copyright law provisions generally, cable being an example.

Senator **Metzenbaum**. If that is the case, then we can strike that language. Is that what you are saying?

Mr. **Gortikov**. I cannot respond to you. I will get a complete answer on the antitrust provisions.

Senator **Mathias**. While you were responding to the rollcall vote, Dr. Greenspan testified on the profit question in some detail and I think it would be helpful for you to review his testimony.

Senator **Metzenbaum**. But while you were also responding, I read from the footnote we found in the audio recording coalition, footnote 14, indicating how well RCA records was doing, Consumer Electronics Division, boosting record profits, WCI Record Group, including Warner, Elektra, Asylum, calling 1984 the best year ever.

WCI Record Group posted its highest third quarter records ever, although it should be pointed out that that includes some domestic home video sales.

So what I was saying is, here we have some testimony of Dr. Greenspan, and I am not challenging his credibility at all nor Mr. Gortikov's, but what I am saying is here we have these other figures, and until we know what the mix is, and why it came about, you know, there may be one or two companies that took a real bath.

Senator **Mathias**. Senator Leahy.

OPENING STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Senator **Leahy**. I apologize for not being here earlier, but, as I mentioned to the chairman, we have had a matter of some urgency in the Intelligence Committee that has kept us over there with the Secretary of State most of the morning.

I would like to begin by asking this question: according to the Recording Industry Association of America, the number of new albums released has fallen by about half since 1978. That was during a period of record profits for the industry. The number of albums has gone down, profits have gone up. Why?

Dr. GREENSPAN. First, let me respond in part, because this is not unrelated to the question Senator Metzenbaum raised.

As best I can judge, Senator, the record industry profit broke even in 1983 and exhibited a small profit in 1984. Margins are well below where they were for domestic operations in the period prior to when home taping really began to take hold. Profits were up last year, but there were very substantial losses in 1982, 1981, and 1980. The best I can judge, looking at the fairly broad sample, it does not appear that there are just a few individual companies that are doing exceptionally badly and holding the average down.

As best I can judge, that is not the case. At the moment there are a lot of companies who are in a loss position. There are some who are breaking even; there are some who are making moderate profits, and there are some who are probably doing quite well. However, the overall average is one clearly significantly below that which prevailed prior to the onset of major acceleration in home taping in the latter part of the 1970's. In that sense, Senator Leahy, the decline in new recordings is more a reflection of the declining profitability of the industry, because as Mr. Gortikov testified, a relatively small fraction of records that are released are profitable.

The trouble is, you do not know in advance which ones will be profitable and which will not be. What those data tell us is that the willingness to take risks on the part of the record industry is substantially reduced. What in effect those numbers are telling us is that the record companies increasingly cannot afford to take the risks.

Senator LEAHY. If indeed there are only half the number of albums being released today as there were 5 or 6 years ago, what kind of titles are being dropped?

Mr. GORTIKOV. I cannot give you precise answers to that, Senator. Every company that puts out a recording anticipates a profitable result when it puts out that recording.

Senator LEAHY. But you must have some idea of the type of titles that have been dropped.

Mr. GORTIKOV. I could get that for you. I do not know the facts. Those that might enjoy only a moderate sale in the past, my guess is, having been a record company president myself, that those would be passed by.

Senator LEAHY. We can look at the actual titles when you send them to me, but I would suggest that we will find that titles like the Brandenburg Concerto are more likely to be dropped than the soundtrack of Miami Vice. I would also suggest that the one more likely to be taped at home by the teenagers who do so much of the taping is the soundtrack of Miami Vice and not the Brandenburg Concerto.

I want to see the numbers and titles before I draw a conclusion, but I suspect that home taping is not the only reason why so many titles are being dropped.

Mr. GORTIKOV. That is correct, and also those who tape are not just teenagers. They go into other higher age categories as well.

Senator LEAHY. Old people like myself.

Mr. GORTIKOV. It might also be interesting to examine the profitability of the tape companies, the companies that are putting out tapes on the chart you saw, and the companies putting out the machines.

Senator LEAHY. I have every intention of asking those questions, because I do want to find out where some of the value of these recordings go. Do they go to Japanese electronics companies or do they go to American artists? And I do not mean that in a pejorative sense.

If the New York Philharmonic Orchestra makes a record today, how much goes to the orchestra, how much to the composer—assuming it was a contemporary composer—and how much goes to the music publisher?

Mr. GORTIKOV. Well, that varies all over the lot by individual contract. The royalties paid to recording artists are very wide ranging. The royalties gained by music publishers and composers are pretty close to a statutory rate.

Senator LEAHY. Maybe I could put it this way. Would you distribute the profits the same way if you had on the one hand Michael Jackson, the New York Philharmonic on the next, and a good friend of mine, John Gailmore, on the third?

Mr. GORTIKOV. Because of bargaining power, Michael Jackson would require a much higher royalty than the next artist you mentioned. The New York Philharmonic probably does a pretty good job of negotiating its royalty rate, although in most cases the issuance of classical recordings is a subsidy on the part of the record company, as most of those do not yield a profit.

Senator LEAHY. My time is up, but I would like to ask you how the royalty fees would be distributed.

Mr. GORTIKOV. This bill provides that regulations would be set up for the distribution of those moneys, and undoubtedly the parties would bring to that government-regulated entity an agreement as to the sharing of royalties. Essentially, the basic principle is that sales are being displaced by home taping, and these various constituencies are deprived of x shares of that legitimate sale that was displaced. The sharing of royalty would basically track the revenue that was displaced by home taping.

Senator LEAHY. Thank you, Mr. Chairman.

Senator MATHIAS. Thank you, Senator Leahy. We need to move on to the next panel, but I have one further question. This bill provides for an exemption for equipment that contains technological innovations which would prevent unauthorized home taping.

Is there any likelihood that the marketplace would take care of this problem? Are there technological solutions that are either available now or just over the horizon that would respond to the home taping problem?

Mr. GORTIKOV. Yes, Senator, in your absence again, I did describe precisely one such technological capability, but that would allow a subliminal signal within the recording itself that would require a compatible chip in the taping mechanism. This would prevent the copying of a specific recording but would clearly permit the recording of a noninfringing product. A recording company could charge extra for its recording that could permit taping to offset the loss of sale. It might keep that inaudible signal out of the recording and sell the record for more. So there is a technological solution that would require a mandatory chip in the taping equipment, which would probably in turn require a law.

Dr. GREENSPAN. Senator, I also suspect that when confronted with this legislation you will begin to find that there emerges a fairly substantial spread among the types of blank tapes produced, because of the incentive to produce tapes which would be clearly not subject to copyright infringement. A lot of the ambiguity which now exists in the current market would probably disappear as a result of market adjustments themselves. This legislation is adequate, in my judgment, to create that type of an incentive.

Senator MATHIAS. Thank you very much. I appreciate your being with us.

Senator LEAHY. I wonder if I could have permission to submit a number of questions in writing.

Senator MATHIAS. I am glad you reminded me, because I would like to ask the witnesses if they would respond to questions in writing, because we have had to limit the time.

[The following joint statement was received for the record:]

SUMMARY STATEMENT OF NATIONAL MUSIC PUBLISHERS' ASSOCIATION, INC., RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC., AND SONGWRITERS GUILD OF AMERICA

SUBCOMMITTEE ON PATENTS, COPYRIGHTS AND TRADEMARKS
SENATE COMMITTEE ON THE JUDICIARY
OCTOBER 30, 1985

Home taping is a problem of enormous and growing dimensions. Survey evidence demonstrates that Americans tape the equivalent of 564 million albums of music annually --an activity which results in lost sales of records and prerecorded tapes of 325 million albums each year. Dr. Alan Greenspan has estimated that this sales displacement resulted in lost revenues by the American music community of about $1.5 billion in 1984 alone.

What this means is that manufacturers and importers of the tapes and recording equipment that make home taping possible have found a way to appropriate to themselves the benefits of American musical creativity. This appropriation is not benign; ironically, although the success of tape and equipment manufacturers is dependent on the vitality of the American music community, it comes at the direct expense of that community and of the public.

Home taping causes damage to the music industry because sales revenues are the sole source of income for recordmakers and the primary source of income for other music creators and copyright owners. Sales displacement thus undermines the economic security of the industry's hundreds of thousands of working people, and stunts careers for creators at every level of the music community.

Consumers are also harmed by home taping. The loss of revenues it causes leaves the music industry less money to invest in new music, new talent, and new forms of musical expression. That's one of the reasons why, as RIAA statistics show, the number of new albums released has plummeted by almost half since 1978. That means less musical choice for the public. Home taping also means less music because it undermines the fundamental premise of our copyright system: that payment for the use of creative works both rewards the creator for his labor and serves as an incentive for further creativity. By denying to copyright owners compensation for the consumption of their intellectual property, home taping diminishes the incentive to invest time, effort and money in the high risk music industry, and ultimately decreases the amount of music that will be produced.

In addition, home taping is sapping one of the few American industries that has long had a positive effect on our international trade balance. Although American music has been the most sought-after music in the world, worldwide home taping has reduced the flow of revenues into the U.S. and undermined the industry's ability to produce musical products for export. At the same time, the largely foreign manufacturers of tapes and taping equipment have profited handsomely at American expense; imports of both tapes and taping equipment have more than tripled since 1980.

The Home Audio Recording Act provides a fair and workable solution to the home taping problem. By placing a modest royalty on blank tapes and recording equipment, the Act accomplishes two fundamental goals: it ensures that the creators of our nation's musical heritage will receive a reasonable return for their creative efforts, and at the same time permits music lovers to continue to tape music for their own use free of infringement liability.

The Act improves upon previous versions of home taping royalty legislation to respond to problems identified in prior hearings and debate. First, the Act applies to home music taping only; home video taping is not affected. Second, the Act specifies the amount of the royalty that will be placed on both blank tape and equipment, rather than leaving calculation of the assessment to later, uncertain negotiation. Finally, the Act fashions new protections for those who tape noncopyrighted material.

The essence of the bill remains unchanged, however, and strikes at the heart of the home taping problem. By passing it, Congress will follow the lead of many other countries that have enacted home taping legislation. At least ten foreign nations have already established a royalty system to compensate the creators and producers of their music, and twelve others are moving in the same direction.

The continued protection of our nation's musical heritage demands no less. We urge the Congress to enact the Home Audio Recording Act without delay.

JOINT STATEMENT
OF
NATIONAL MUSIC PUBLISHERS' ASSOCIATION, INC.
RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC.
AND
SONGWRITERS GUILD OF AMERICA

RE: S. 1739

THE HOME AUDIO RECORDING ACT

BEFORE THE SUBCOMMITTEE ON
PATENTS, COPYRIGHTS AND TRADEMARKS
OF THE
SENATE COMMITTEE ON THE JUDICIARY

- - - - - - - - - - - - -

October 30, 1985

AUDIO HOME TAPING: THE CASE FOR A FAIR DEAL FOR CREATORS AND CONSUMERS

SUMMARY OF POSITION

The National Music Publishers' Association, the Recording Industry Association of America, and the Songwriters Guild of America join the entire musical arts community -- including the 1,300 companies and more than 2.5 million individuals who have formed a Coalition to SAVE AMERICA'S MUSIC* -- in supporting prompt passage of the Home Audio Recording Act. The Act accomplishes two fundamental goals: it frees individuals from copyright liability when they tape music for their private enjoyment, and at the same time ensures that music creators and copyright owners will receive some compensation for the fruits of their endeavors. It represents a much needed compromise solution to a massive and growing problem: the home taping of copyrighted musical recordings.

The Home Taping Problem

Sophisticated audio recording technology now enables the individual, privately and at the push of a button, permanently to capture a copyrighted musical performance -- for free. Incredibly, one can today build an entire library of recorded music without ever purchasing a single record.

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*A list of the Coalition's membership is attached as Appendix One.

The appeal of blank tape and taping equipment is predicated principally on their ability to copy musical recordings, as the advertisements for those products so clearly indicate. Indeed, much of this promotional literature -- some of which is displayed in the following pages -- exhorts consumers to "beat the system" by copying music from borrowed cassettes.

In essence, the manufacturers and importers of blank tape and taping equipment have found a way to appropriate to themselves the benefits of American musical creativity. In doing so, they are not simply capitalizing on our skills, labors, and investments; they are damaging us in the process, for when our music is taped instead of bought, the sales which are the lifeblood of our industry are displaced. Thus, the success of the tape and equipment manufacturers -- which is dependent on the vitality and appeal of our music -- comes at the direct expense of the American music community, and ultimately the American public.

Statistics tellingly reveal the dimensions of this problem. Audit & Surveys, an internationally respected market research firm which conducted a comprehensive study of the home taping phenomenon in 1983, found that

- -- Americans tape the equivalent of 564 million albums of music annually.
- -- Home taping results in lost sales of records and prerecorded tapes equivalent to 325 million albums annually.
- -- At least 84 percent of blank tapes are used to record music.

The scope of this problem will only be exacerbated by new technological developments. The recent introduction of compact discs is likely to lead to a rush to copy from high quality masters; the development and growing use of dual cassette machines will only facilitate increased copying. Now there is even the threat of triple cassette machines on the horizon. Increased home taping will be the inevitable result.

The Consequences of Home Taping

The home taping that results from "beating the system" has exacted huge costs from both the music community and consumers around the country. Dr. Alan Greenspan, former Chairman of the President's Council of Economic Advisers, has estimated that the displacement of sales of prerecorded music caused by home taping resulted in lost sales revenues by the American music community of about $1.5 billion in 1984 alone. These sales are the sole source of income for recordmakers and the primary source of income for other music creators and copyright owners. Not only do these losses affect the viability of the music industry; they also undermine the economic security of the hundreds of thousands of working people across the country -- technicians, musicians, writers, performers and producers, to name but a few -- whose livelihood depends on the continued sales of albums and prerecorded cassettes. Home taping also means reduced opportunities and stunted careers for creators at every level of the music community.

It is consumers who are ultimately harmed by home taping. The loss of revenues it causes leaves the music industry less money to invest in new music, new talent, and new forms of musical expression. That's one of the reasons why, as RIAA statistics show, the number of new albums released has plummeted by almost half since 1978. That means less musical choice, and less music, for the public. Record buyers are also injured -- because the reduced volume of sales, and consequent increase in the per-unit cost of each album sold, can lead to higher prices for records and prerecorded tapes.

The nation as a whole suffers because home taping is sapping one of the few American industries that has traditionally made a positive contribution to our international balance of payments. Although American music has long been the most sought-after music in the international marketplace, worldwide home taping has reduced the flow of revenues into the United States and undermined the industry's ability to continue to produce musical products for export. At the same time, the largely foreign manufacturers of tapes and taping equipment have profited handsomely at American expense; imports of both blank tapes and taping equipment have more than tripled since 1980.

Uncompensated home taping, at bottom, undermines the fundamental premise of our copyright system: that payment for the use of creative works both rewards the creator for his labor and serves as an incentive for further creativity. By denying to copyright owners compensation for their work -- for the consumption of their intellectual property -- home taping diminishes the incentive to invest time, effort and money in the high risk music industry, and ultimately decreases the amount of music that will be produced for the public to enjoy.

The Solution to the Home Taping Problem

The Senate now has before it S. 1739, the Home Audio Recording Act, which provides a fair and workable solution to the home taping problem. By placing a modest royalty on the sale of blank tapes and recording equipment, the bill accomplishes two fundamental objectives: it ensures that the creators of our nation's musical heritage will receive a reasonable, if partial, return for their creative efforts, and at the same time permits music lovers to continue to tape music for their own use, unfettered by liability for copyright infringement.

The Act differs in significant respects from previous versions of home taping royalty legislation, and incorporates improvements that respond to problems identified in Congressional hearings and debate on prior bills. First, the Act applies to home music taping only; home video taping is not affected. Second, the Act specifies the amount of the royalty that will be placed on both blank tape and equipment, rather than leaving calculation of the assessment to later, uncertain negotiation. Finally, the Act fashions new protections for those who tape noncopyrighted material. Under the Act, the Copyright Royalty Tribunal is given the authority to exempt from any royalty whatsoever (i) tapes and equipment "unsuitable" for music taping on the basis of technical criteria (such as reproductive quality), and (ii) tapes and equipment used in a trade, business or profession for purposes other than personal music taping. Thus, dictation equipment and microcassettes will be exempt from royalties, as will tapes purchased for noninfringing purposes, such as classroom instruction, broadcasting, or programming for the blind and disabled.

The essence of the bill remains unchanged, however, and strikes at the heart of the home taping problem. By passing it, Congress will follow the lead of many other countries that have enacted home taping legislation. At least ten foreign nations, including France, West Germany, Austria and several Scandinavian countries, have already established a royalty system to compensate the creators and producers of their music, and twelve others are moving in the same direction. The Government of the United Kingdom, for instance, recently proposed that a royalty be added to the sale of blank audio tapes, and a subcommittee of Canada's House of Commons this month recommended adoption of a royalty on both tapes and taping equipment.

We urge the Congress to act now to save America's music. The Home Audio Recording Act responds to the challenge posed by new technology with a creative solution that preserves the benefits of that technology for consumers but at the same time protects the rights of music creators. The Act thus achieves notable benefits: it permits individuals to tape music without copyright liability; restores the integrity of our copyright system; contributes to the continued enhancement of our rich musical tradition; and ensures the continued support of an industry that benefits the American economy as a whole. It should be enacted without delay.

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APPENDICES

1. The Coalition To Save America's Music

2. Statement of Alan Greenspan
Re: S. 1739, Before the Subcommittee
on Patents, Copyrights and Trademarks
of the Senate Committee on the Judiciary
(October 30, 1985)

I. HOME TAPING IS MASSIVE AND GROWING

Across the country, millions of people now use audio recorders to tape -- rather than purchase -- prerecorded music. This problem was a massive one in 1982, when the National Music Publishers' Association, the Recording Industry Association of America, and the Songwriters Guild of America first testified before this Committee; it has grown even larger since that time. A manufacturer of taping equipment summarized the problem when it said in a pointed advertisement: "one look at the Sharp Tape Factory and you can understand why there's trouble in the music industry."

A. Home Taping is Already Massive

That home taping has already reached massive proportions is undeniable. A comprehensive study conducted in 1983 by Audits & Surveys, an internationally respected market research organization,[1] found that

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[1] The Audits & Surveys study (hereinafter cited as "Audits & Surveys Report") was commissioned by the Recording Industry Association of America and submitted to this Committee in 1983. See Video and Audio Home Taping: Hearings Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. at 193-224 (1983) (hereinafter cited as "1983 Senate Hearings"). The study was conducted pursuant to rigorous methodological standards. Unlike previous home taping studies, moreover, the Audits & Surveys study did not rely upon tapers' recollections. Instead, it measured actual behavior, using contemporaneous individual diaries, follow-up interviews, and in-house audits. A description of the methodology employed follows the study itself. See Audits & Surveys Report at 25-32.

Americans tape the equivalent of 564 million albums of music annually -- a market value of more than $3.8 billion worth of music. (See chart on page 3.) Indeed, as much music is now taped as is bought.[2]

B. Equipment and Tape Sales Are Growing

Home taping has been fueled by the growing availability, at low cost, of sophisticated recording equipment that is also easy to operate. The steadily declining cost of tapes and taping equipment has made taping increasingly accessible and attractive.

In 1969, about one-quarter of U.S. households owned audio recording equipment. By 1977, that figure had increased to 40 percent. By 1984, more than 60 percent of all American households owned such equipment. This represented ownership of 91 million units of recording equipment, a number that grows by 25 to 28 million units each year.[3]

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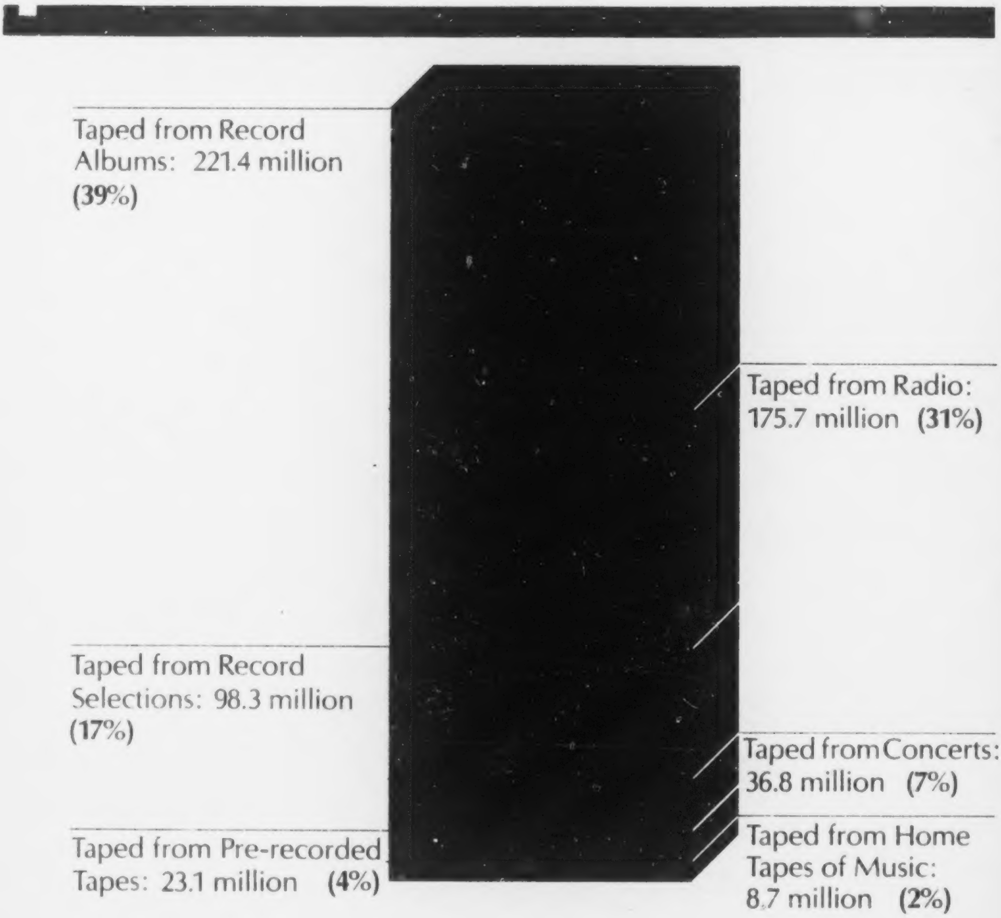
[2] In 1984, manufacturers' shipments amounted to 574 million album equivalents. See Recording Industry Association of America News Release, April 1, 1985.

[3] See Statement of Alan Greenspan Re: S. 1739 (October 30, 1985) at 2 (hereinafter cited as "Greenspan Statement"; attached as Appendix Two).

Annual Volume of Music Taped



Source: Taping Diaries

Most of that recording equipment is imported from the Far East. Between 1980 and 1984, the value of tape recorders imported into the United States more than tripled -- from $1.6 billion to $5.3 billion.[4]

This increase in sales of recording equipment has been more than matched by the growth in blank-tape sales, as the chart on page 5 demonstrates. In 1971, about 4.4 billion minutes of blank audio tape were shipped for sale. In 1984, Americans were offered 19.6 billion minutes of blank tape -- an increase of 345 percent.[5] In 1984, furthermore, the value of blank tape imported into the United States ($710 million) was more than three times higher than the value of blank tape imported just four years earlier ($229 million).[6]

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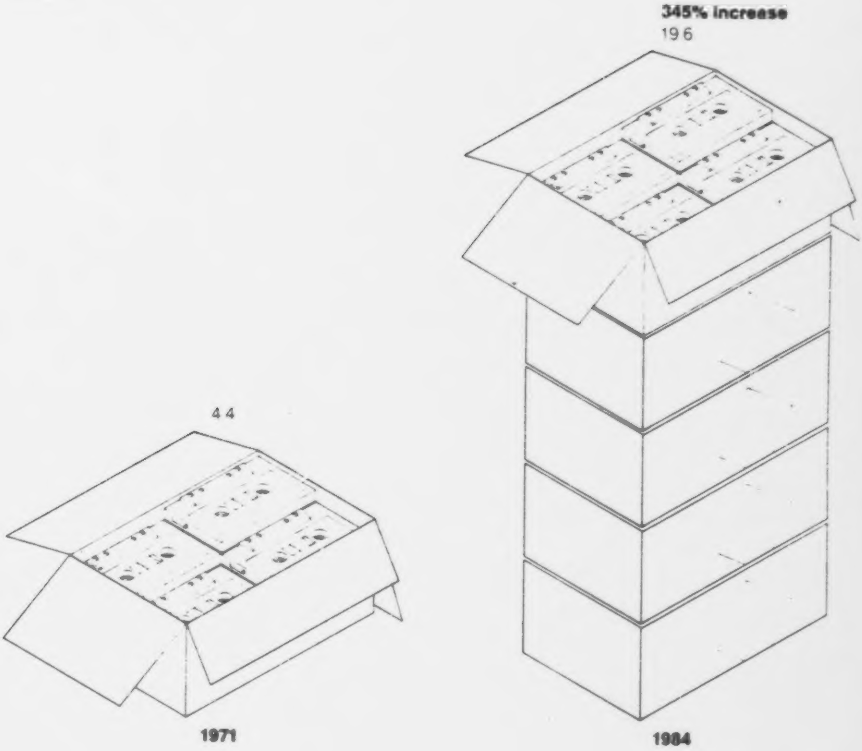
[4] U.S. Department of Commerce, Annual Data on U.S. Imports and Exports for Selected Commodities Groups, 1980-1984.

[5] *Compare* "Blank Tape Spotlight," *Billboard*, August 26, 1972 at 44, 48, *with* *Merchandising Magazine*, March 1985 at 94.

[6] U.S. Department of Commerce, Annual Data on U.S. Imports and Exports for Selected Commodities Groups, 1980-1984.

Blank Tapes Shipped for Sale
(in billions of minutes)



C. Home Taping Will Continue To Grow

Home taping has been rising at a very substantial pace in recent years. Assuming only a single use of a new blank tape, economist Dr. Alan Greenspan has found that in 1972 home taping accounted for 20 percent of the total hours of recorded music available from both purchase and taping. By 1977, this figure had increased to 32 percent. In 1984, home taping accounted for a full 40 percent of the total hours of all recorded music.[7]

Other studies confirm that home taping of music is growing. A survey conducted by CBS Records in 1979 found that 55 percent of the persons purchasing blank tape stated that they were engaging in more taping that year than they had in the previous year.[8] Similarly, a study performed by Warner Communications, Inc. in 1982 found significant increases between 1977 and 1980 in the percentages of the population that had access to recording equipment, that bought blank tape, and that engaged in audio taping.[9]

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[7] Greenspan Statement at 4-5; Table 3.

[8] CBS Records, "Blank Tape Buyers: Their Attitudes and Impact on Prerecorded Music Sales," at 10 (Fall 1980) (hereinafter cited as "CBS Survey"). The CBS Survey has previously been submitted to this Committee. See Copyright Infringements (Audio and Video Recorders): Hearings Before the Senate Comm. on the Judiciary, 97th Cong., 1st and 2d Sess. 848-64 (1981 & 1982) (hereinafter cited as "1981 & 1982 Senate Hearings").

The dimensions of the home taping problem will increase as consumers' inventories of tapes and recording equipment grow. Indeed, the vast number of tapers who cite cost as a primary reason for taping[10] have an incentive to use their taping equipment as much as possible. As Dr. Greenspan has noted, the already low cost of taping in effect decreases as inventories of blank tapes and taping equipment grow: once the fixed cost of the equipment has been paid and the equipment is in place, the out-of-pocket costs of taping music become very low -- the cost of the blank tape.[11] Because the ownership of taping equipment has, as shown above, grown dramatically, the initial outlay for taping equipment presents a barrier for fewer and fewer consumers. Increased home taping is the inevitable result.

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[9] Warner Communications, Inc., "A Consumer Survey: Home Taping," at 4-6 (March 1982) (hereinafter cited as "WCI Survey"). This study has been submitted to this Committee. See 1981 & 1982 Senate Hearings at 775-826.

[10] See CBS Survey at 11; WCI Survey at 17. Indeed, a study prepared for the Electronics Industries Association ("EIA"), a predominant force behind opposition to the proposed legislation, confirms that an overwhelming majority of tapers cite lower cost as a reason for preferring home tapes over prerecorded music. See Yankelovich, Skelly & White, "Why Americans Tape," reprinted in Home Recording of Copyrighted Works: Hearings Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Comm. on the Judiciary, 97th Cong., 2d Sess at 927-1032 (1982) (hereinafter cited as "YSW Report"). This is hardly surprising; Dr. Alan Greenspan has noted that in 1984 the total cost of home taping was only $1.67 per album equivalent, or 25 percent of the equivalent price of prerecorded tapes and records ($6.80). Greenspan Statement at 4.

These trends will only be exacerbated by the fruits of new technology that are now appearing in the American marketplace. The increasing availability of compact discs, for instance, is likely to increase the volume of music that is taped annually for two reasons. First, compact discs provide the equivalent of an original master recording from which high quality home tapes can be made.[12] Second, because compact discs are more costly, the price differential between buying and taping is even greater, making low cost taping even more appealing.

In addition, equipment that is specifically designed to facilitate home taping has recently emerged as a strong force in the United States market. When the Recording Industry Association of America appeared before this Committee in October 1983, it demonstrated the use of one of the handful of dual cassette machines then on the market. Now, just two years later, 254 different models of these dual cassette machines are manufactured by some 56 different companies. Not surprisingly, these varied models are gaining a significant share of the market for taping equipment: 24% of cassette tape deck components purchased today are dual cassette machines.[13] And that number is likely to grow: according to a market survey conducted by Matsushita Electric, the number of radio/cassette recorders produced in Japan with twin decks increased from 11% to 30% of the total between 1983 and 1984, and it is expected that the percentage will hit the 60% mark in 1985.[14]

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[11] Greenspan Statement at 3.

[12] Indeed, this Committee has itself recognized that a compact disc is a "high quality recording that is particularly suitable for reproduction." See S. Rep. No. 98-162, 98th Cong., 1st Sess. at 3 (1983) (Record Rental Amendment of 1983).

Now, a Japanese equipment manufacturer has introduced a triple deck machine. (See page 10.) The manufacturer boasts that this new triple deck device

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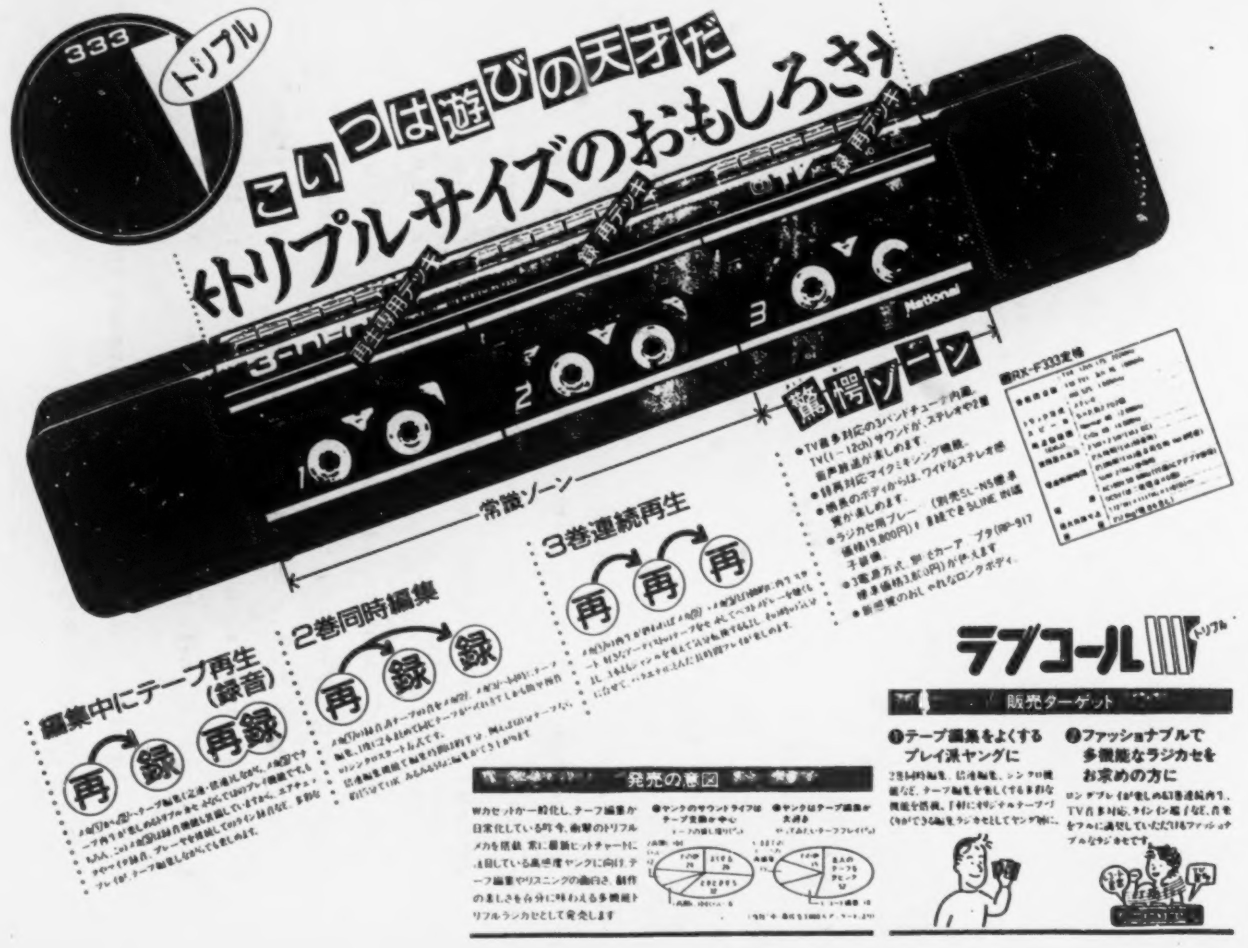
[13] "EIA Audio Industry Consumer Study: Purchased Ownership Patterns of Home and Car Audio Equipment, 1980-1982-1984," Market Facts, March 1985 at 31.

[14] "Japanese Twin Deck Boom," Billboard, August 3, 1985 at 85.


333
トリプル
再生専用デッキ
録・再デッキ
録・再デッキ
National
1
2
3

こいつは遊びの天才だ

《トリプルサイズのおもしろさ》

常識ゾーン

驚愕ゾーン

3巻連続再生

再→再→再

2巻同時編集

再→録→録

編集中にテープ再生（録音）

再→録　再録

- ●TV音多対応の3バンドチューナ内蔵。TV(1－12ch)サウンドが、ステレオや2重音声放送が楽しめます。
- ●録再対応マイクミキシング機能。
- ●横長のボディからは、ワイドなステレオ音質が楽しめます。
- ●ラジカセ用プレー（別売SL-NS標準価格19,800円）を接続できるLINE IN端子装備。
- ●3電源方式、車でカーアダプタ(RP-917標準価格3,800円)が使えます
- ●新感覚のおしゃれなロングボディ。

■RX-F333定格

ラブコールIII トリプル

販売ターゲット

❶テープ編集をよくするプレイ派ヤングに

2巻同時編集、追っかけ編集、シンクロ機能など、テープ編集を楽しくする多彩な機能を搭載。「手軽にオリジナルテープづくりができる編集ラジカセ」としてヤング層に。

❷ファッショナブルで多機能なラジカセをお求めの方に

ロングプレイが楽しめる3巻連続再生、TV音多対応、ラインイン端子など、音楽をフルに満喫していただけるファッショナブルなラジカセです。

発売の意図

Wカセットが一般化し、テープ編集が日常化している昨今、衝撃のトリプルメカを搭載。常に最新ヒットチャートに注目している高感度ヤングに向け、テープ編集やリスニングの面白さ、操作の楽しさを存分に味わえる多機能トリプルラジカセとして発売します

●ヤングのサウンドライフはテープ重視が中心

●ヤングはテープ編集が大好き

makes it easy to make two copies of the same tape.[18]

D. Tape and Equipment Manufacturers and Importers Encourage Increased Home Taping

Manufacturers and importers of blank tapes and taping equipment have been quick to capitalize on the capability of their products to copy prerecorded music, without any regard to the devastating impact those products are having on the American music community. Their advertisements stress the unique suitability of their particular brands of tape to make high-quality music reproductions. Manufacturers claim that theirs is "the most musical cassette tape," that theirs are specially formulated for "digital audio music recording," and that theirs are "for people who want to do some serious taping." One manufacturer urges customers to "take the brilliant sound quality" of compact discs to the beach by taping them onto 90-minute cassettes; another urges tapers to double their "music money rebate" by purchasing extra blank tapes. (See pages 12-17 for a sampling of their ads.)

Advertisements for taping equipment encourage home taping even more blatantly, by exhorting consumers

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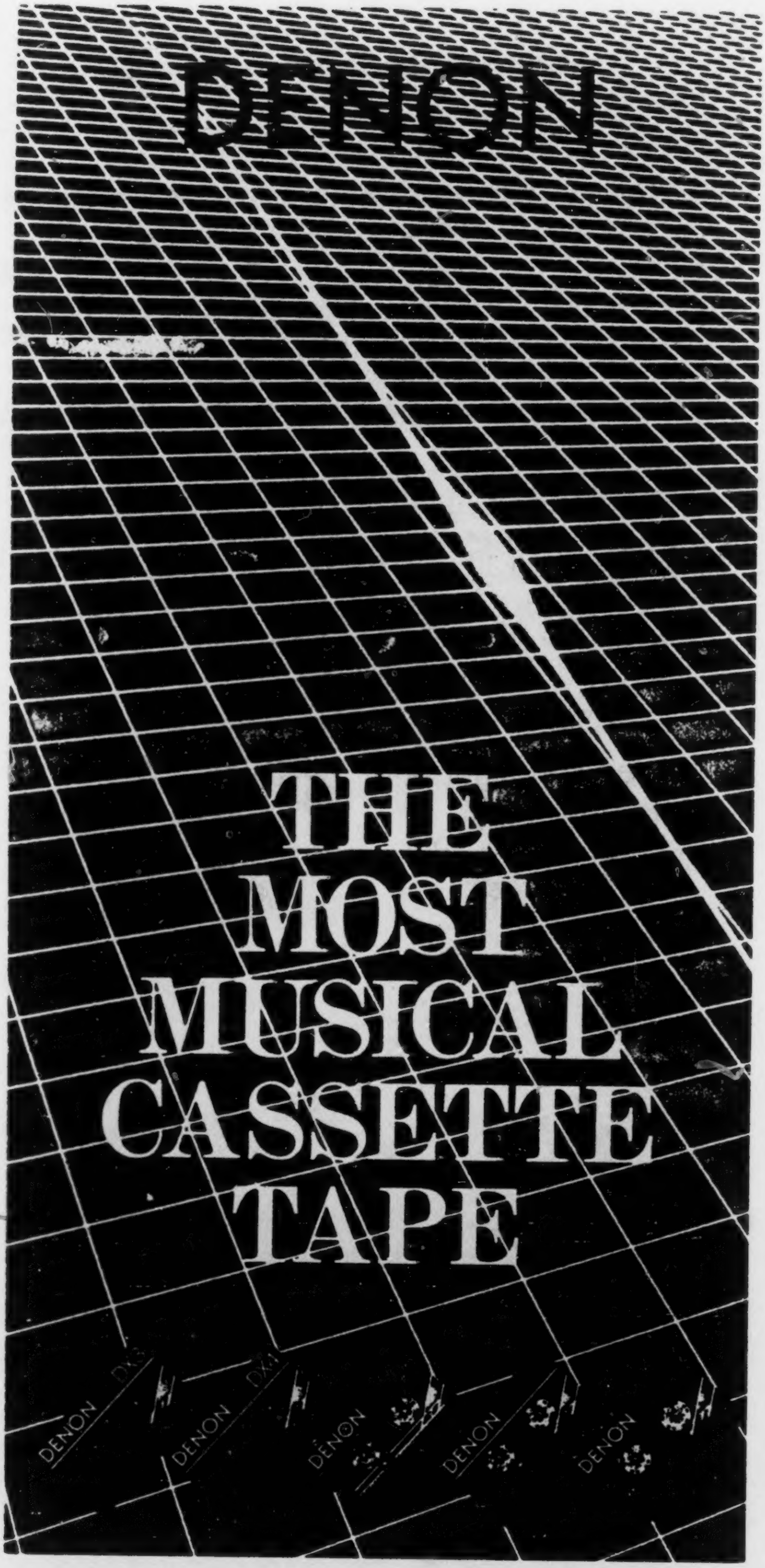
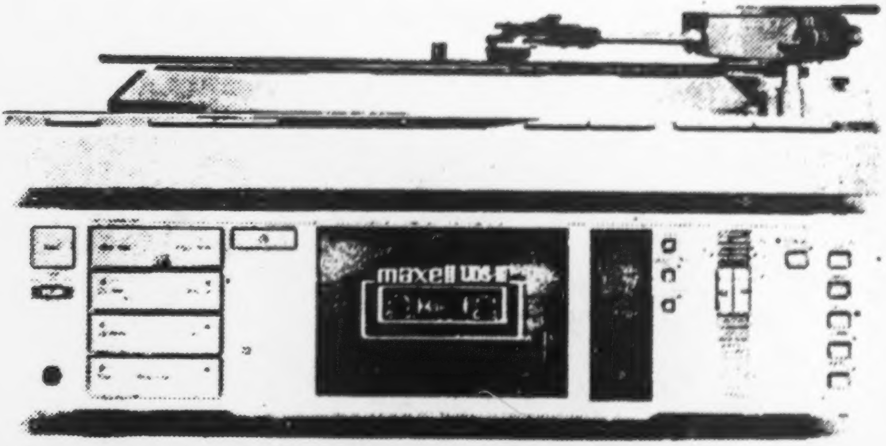
[18] "Matsushita Triple-Decker to Hit Japanese Market," Billboard, July 27, 1985 at 73.


DENON
THE MOST MUSICAL CASSETTE TAPE
DENON DX3
DENON DX1
DENON
DENON
DENON


maxell UDS-II

INTRODUCING MAXELL UDS.
FOR PEOPLE WHO WANT TO DO
SOME SERIOUS TAPING.

Finally, you can afford to put your entire record collection on cassettes you'll actually want to listen to.

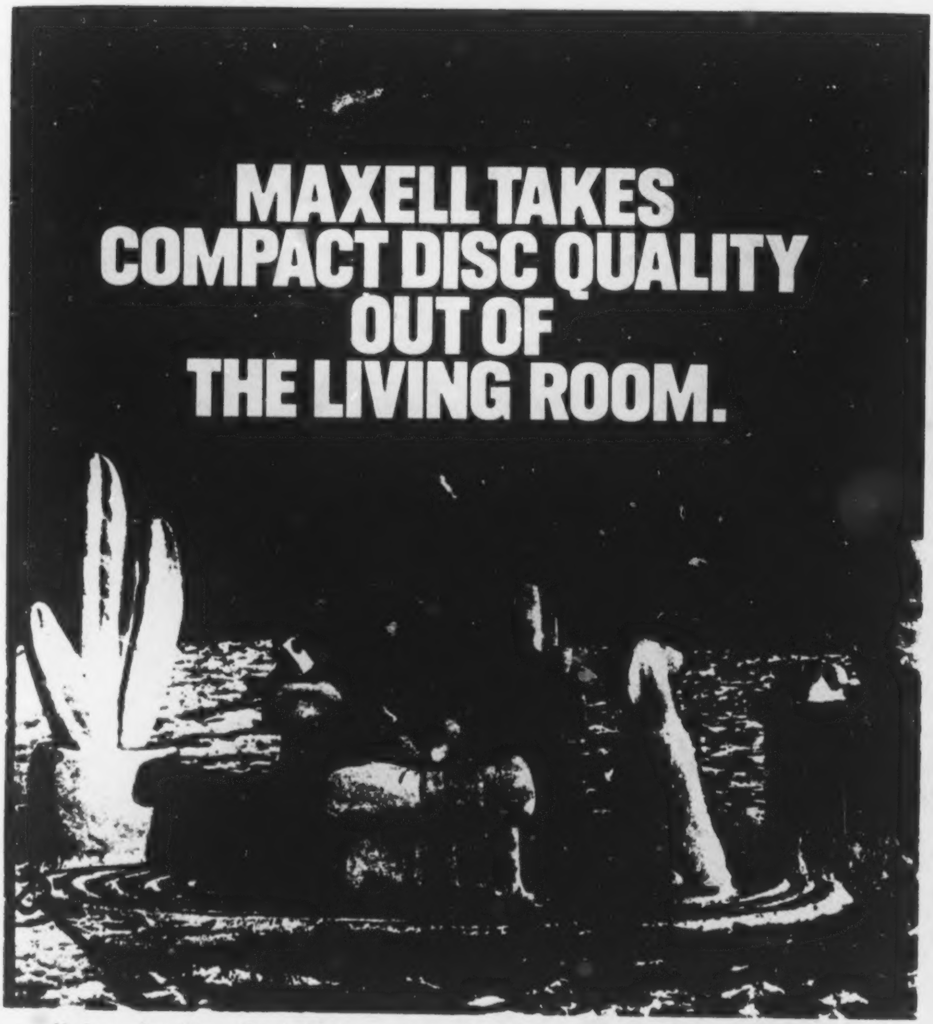
Maxell's new UDS.

maxell UDS-II

IF YOU
COULD HEAR
THIS TAPE,

90
FOR CD & DIGITAL AUDIO MUSIC RECORDING
MEMOREX
MEMOREX® CDX II
METAL TAPE FOR HIGH BIAS/CRO2 SETTING

© 1985 Memtek Products



Ah, the comforts of home. They're tough to leave behind. Especially when it comes to things like your compact disc player.

But even though you might not be able to take the player with you, you can take the brilliant sound quality. If you record your compact discs on Maxell XL-S cassettes.

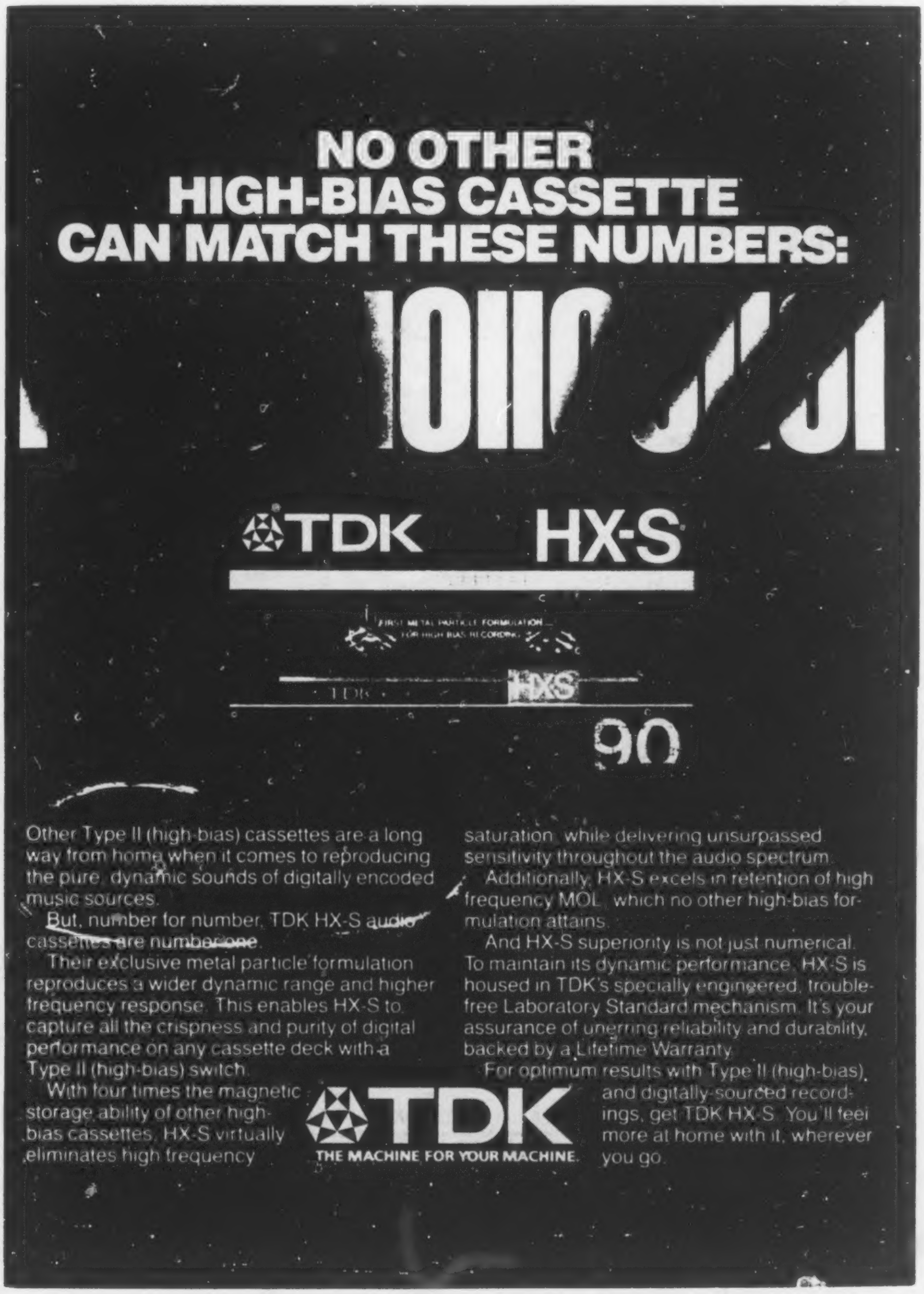
By producing smaller, more uniform magnetic particles, we can pack more of those particles on the tape surface. Which makes it possible to record more information on a given area of tape.

As a result, AC bias noise is greatly reduced. And maximum output levels are significantly increased. In fact, the dynamic range of XL-S is expanded so much, it can capture everything from the subtle passages to the extreme bursts inherent to compact discs.

So record your compact discs on Maxell XL-S.

Then you can enjoy their sound quality wherever you feel at home.

IT'S WORTH IT.



NO OTHER HIGH-BIAS CASSETTE CAN MATCH THESE NUMBERS:

Other Type II (high-bias) cassettes are a long way from home when it comes to reproducing the pure, dynamic sounds of digitally encoded music sources.

But, number for number, TDK HX-S audio cassettes are number one.

Their exclusive metal particle formulation reproduces a wider dynamic range and higher frequency response. This enables HX-S to capture all the crispness and purity of digital performance on any cassette deck with a Type II (high-bias) switch.

With four times the magnetic storage ability of other high-bias cassettes, HX-S virtually eliminates high frequency saturation, while delivering unsurpassed sensitivity throughout the audio spectrum.

Additionally, HX-S excels in retention of high frequency MOL, which no other high-bias formulation attains.

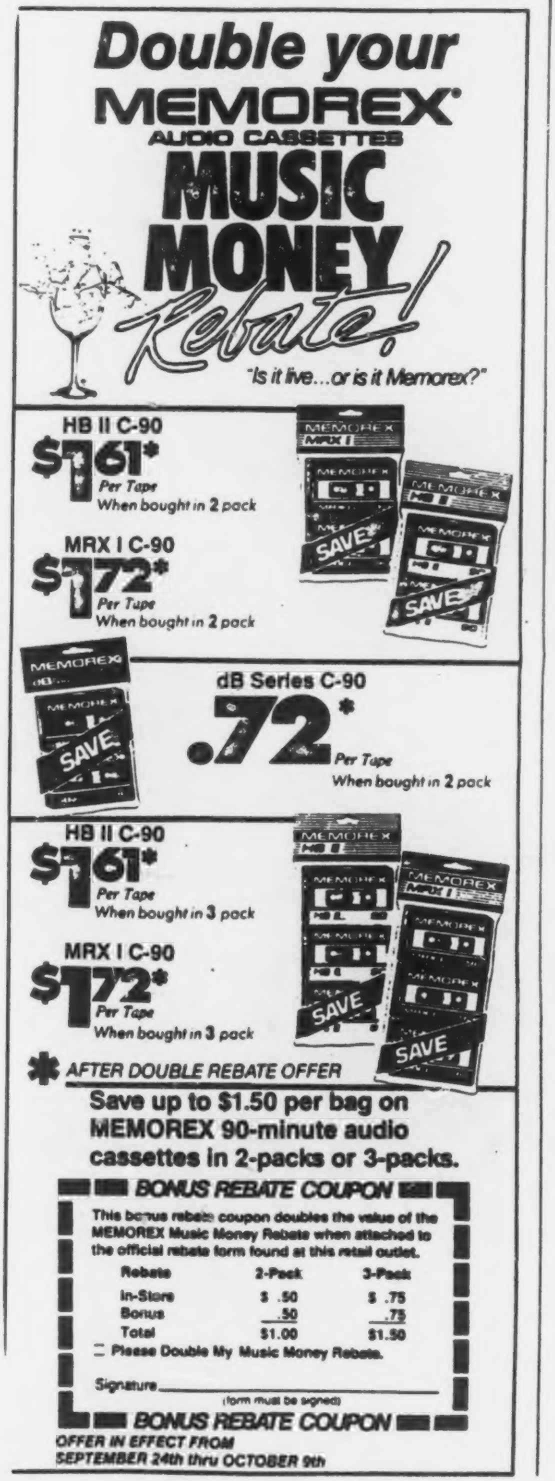
And HX-S superiority is not just numerical. To maintain its dynamic performance, HX-S is housed in TDK's specially engineered, trouble-free Laboratory Standard mechanism. It's your assurance of unerring reliability and durability, backed by a Lifetime Warranty.

For optimum results with Type II (high-bias), and digitally-sourced recordings, get TDK HX-S. You'll feel more at home with it, wherever you go.

TDK

THE MACHINE FOR YOUR MACHINE.

October, 1985 *Pulse!* Page 49



MEMOREX
MRX I
HB II
dB
SAVE

Double your MEMOREX® AUDIO CASSETTES MUSIC MONEY *Rebate!*

"Is it live...or is it Memorex?"

HB II C-90
$1.61*
Per Tape
When bought in 2 pack

MRX I C-90
$1.72*
Per Tape
When bought in 2 pack

dB Series C-90
.72*
Per Tape
When bought in 2 pack

HB II C-90
$1.61*
Per Tape
When bought in 3 pack

MRX I C-90
$1.72*
Per Tape
When bought in 3 pack

* *AFTER DOUBLE REBATE OFFER*

Save up to $1.50 per bag on MEMOREX 90-minute audio cassettes in 2-packs or 3-packs.

BONUS REBATE COUPON

This bonus rebate coupon doubles the value of the MEMOREX Music Money Rebate when attached to the official rebate form found at this retail outlet.

Rebate	2-Pack	3-Pack
In-Store	$ .50	$ .75
Bonus	.50	.75
Total	$1.00	$1.50

☐ Please Double My Music Money Rebate.

Signature____________________
(form must be signed)

BONUS REBATE COUPON

OFFER IN EFFECT FROM
SEPTEMBER 24th thru OCTOBER 9th

to "beat the system" and "save money" by copying "a friend's cassette." One advertiser bluntly suggests, "You have friends. Your friends have friends. Why not pool your resources and dramatically increase your cassette collection with the latest in high speed high quality tape duplicators." Still others advise that their dual cassette recorder "quickly pays for itself by turning inexpensive blanks into prerecorded music cassettes. It's like getting the high quality AM/FM stereo for free." (See pages 19-23.)

Indeed, taping has become such a widely accepted phenomenon that magazines written for college students freely advise them that "with the abundance of record collections in a dormitory, college is the perfect place to expand a personal music collection by copying friends' albums onto cassettes."[16] Some radio stations, furthermore, have long urged their listeners to engage in home taping; WSAC in Elizabethtown, Kentucky, for instance, encourages listeners to tune in to a "mini concert" if "you've ever wanted to tape your favorite

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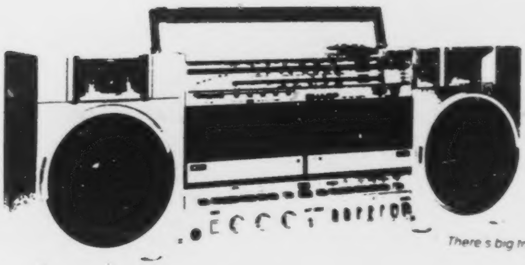
[16] "Sound Advice," Dorm Magazine, Spring 1985 at 26.



Tape Factory

There s big trouble in the music industry

One look at the Sharp Tape Factory and you can understand why there s trouble in the music industry Records aren t selling because people are copying their favorite songs from stereo FM radio stations onto inexpensive cassettes and playing them on everything from their Sony Walkman to their home cassette players The Sharp Tape Factory certainly won t help the recording industry.

Equipped with AM FM and two shortwave bands the Sharp has two high quality cassette stereo recording tape decks The unit can record off any of its radio frequencies or an external turntable or duplicate an existing tape and do it at double speed A special high-quality audio dubbing circuit lets you speed up both cassette decks to duplicate tapes at one-half the time it normally takes And with tape deck to tape deck balanced circuitry your reproduction quality is awfully close to the quality you d expect from a professional studio

If one of your friends has a tape you want to own copy it Or keep duplicate tapes one tape in your car and one at home Start a tape copying service Use the unit in your business to duplicate copies of important messages.

The Sharp Tape Factory makes sense if you re looking for a little more than entertainment from your home stereo cassette system

The two speakers don t separate from the main unit However each speaker actually contains two separate speakers and they produce excellent sound for their small size The entire unit measures 5 x 8 x 22" ; weighs 12 pounds and comes complete with AC power cord There are provisions for 8 D cell batteries (not supplied) and it has volume balance and tone controls A great music machine

Tape Factory (5051CA09 8 00) **$269.95**

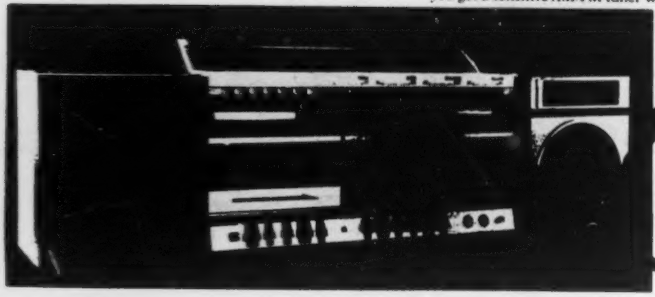
> “If one of your friends has a tape you want to own, copy it. Or keep duplicate tapes — one tape in your car and one at home. Start a tape copying service. Use the unit in your business to duplicate copies of important messages.”

> “One look at the Sharp Tape Factory and you can understand why there's trouble in the music industry. Records aren't selling because people are copying their favorite songs from stereo FM radio stations onto inexpensive cassettes and playing them on everything from their Sony Walkman to their home cassette players. The Sharp Tape Factory certainly won't help the recording industry.”

Beat the system. Copy your own cassettes.

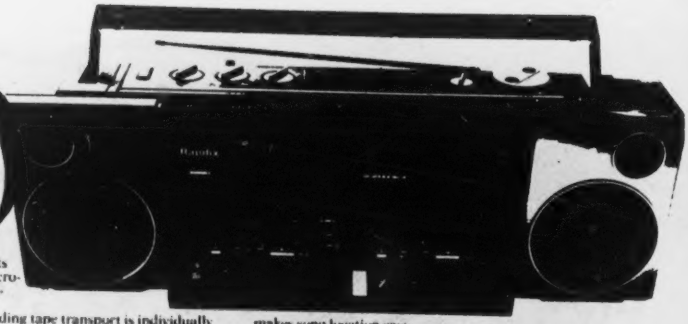
Randix's two directly linked tape decks give you superb direct stereo tape copying capability in one unit. Duplicate a favorite tape for a friend or copy a borrowed cassette.

[illegible] built-in self-adjusting microphones record [illegible] stereo. [illegible] sound with dramatic stereo separation. And the unique Continued Play feature automatically begins second tape when first one plays out. Plus you get a sensitive AM/FM tuner with AFC signal-locking for drift-free radio reception. With slide Volume, Bass/Treble and Balance controls, and inputs for extra speakers, turntable, or tape recorder. [illegible]d-phone jacks. Uses [illegible] batteries (n[illegible] incl[illegible]) with AC cord. [illegible] warranty. [illegible] FCC approved. [illegible]easures 14 × 7 × 6". Weighs 15 lbs.



The Randix portable studio recorder quickly pays for itself by turning inexpensive blanks into prerecorded music cassettes. It's like getting the high quality AM/FM stereo for free.

Randix Studio #LRX200 $199 (4.50).



Su[illegible]d [illegible]ubbing de[illegible]

Randix's new portable *high-speed* dubbing deck lets you make impeccable stereo cassette copies in *half* the normal time. Or tape your favorite radio programs directly from the sensitive built-in AM/FM tuner. Capture live [illegible] [illegible]ngle [illegible]channel has its own built-in condenser microphone. It's a complete mini-studio for less than $150.

Each smooth front-loading tape transport is individually controlled, or can be set for continuous playback from Tape A to Tape B for up to 2 hours of uninterrupted music. Two 4" acoustic suspension speakers produce big, rich sound with dramatic stereo separation. Or use the stereo headphone jack for private listening. Rotary tuning, volume, tone and balance controls are conveniently placed for quick accessibility. 3-digit tape counter makes song location easy.

Pop-up carrying handle lets you take this compact (7H × 21W × 5D") [illegible] [illegible]ABS, weighs 8½ lbs. UL approved. 90 day warranty. Turn inexpensive blank tapes into beautiful music—in half the time.
[illegible]andix Dual Cassette #JRX610 $149 (6.50)

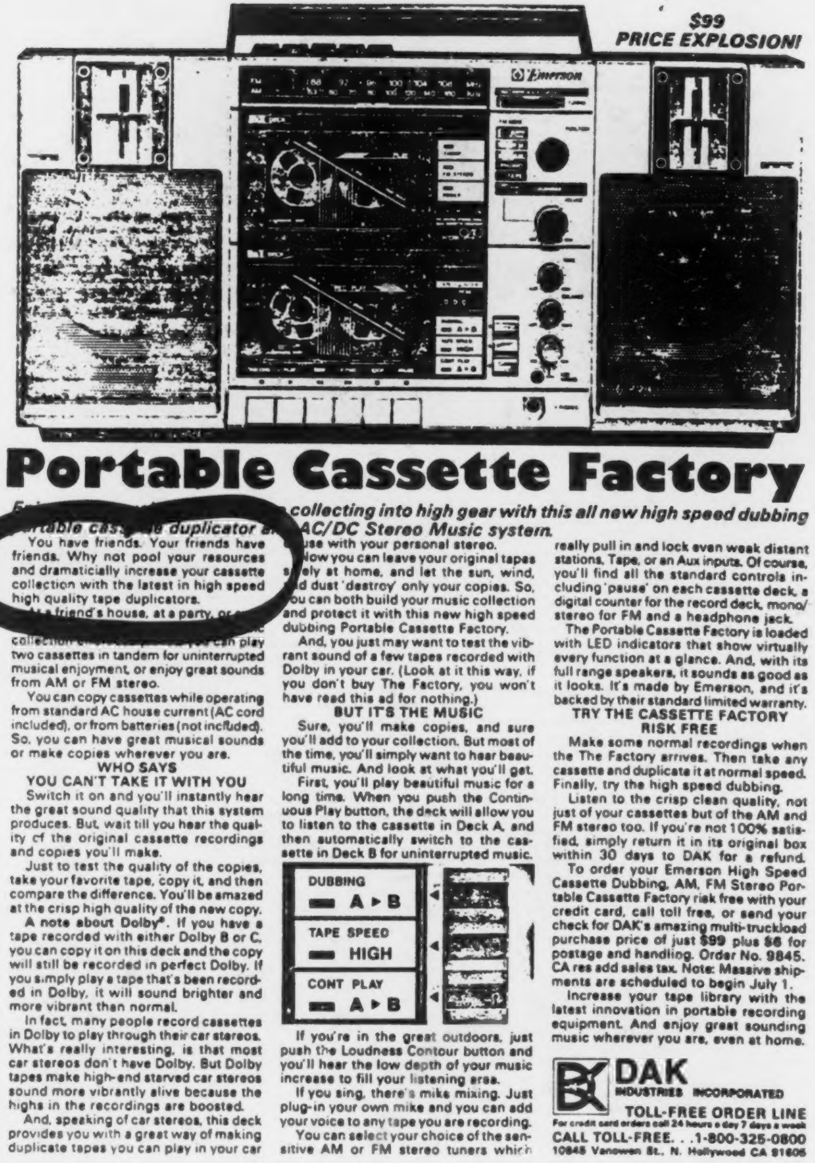
Save Money—Copy A Friend's Cassette ◄

Randix's new twin cassette recorder allows you to copy any tape within minutes. And with its balanced tape deck circuitry, the reproduction approaches the quality obtained in professional recording studios.

A state-of-the-art continuous play function automatically activates a second tape once the first one is finished. So you have double the listening time, without the inconvenience of changing tapes. Two four-way speakers (6" woofers and 2" ceramic tweeters) produce vivid, full range stereo sound. Sensitive AM/FM tuner allows for distortion-free reception. Includes headphone jack, pause button, and a 3-digit tape counter. Plugs into any AC power outlet or uses 6 D batteries (not included). Weighs 14 lbs. UL approved. 90 day warranty.

Order this ultra-compact (21x7x6½") entertainment system today and begin saving money immediately by turning inexpensive blank tapes into high quality stereo cassettes.

■ Randix Twin Recorder SCR*610 $129(6.50)



Portable Cassette Factory

E[illegible] collecting into high gear with this all new high speed dubbing [illegible]rtable cas[illegible]e duplicator a[illegible] AC/DC Stereo Music system.

You have friends. Your friends have friends. Why not pool your resources and dramaticially increase your cassette collection with the latest in high speed high quality tape duplicators.

[illegible] friend's house, at a party, or [illegible] collection [illegible] you can play two cassettes in tandem for uninterrupted musical enjoyment, or enjoy great sounds from AM or FM stereo.

You can copy cassettes while operating from standard AC house current (AC cord included), or from batteries (not included). So, you can have great musical sounds or make copies wherever you are.

WHO SAYS
YOU CAN'T TAKE IT WITH YOU

Switch it on and you'll instantly hear the great sound quality that this system produces. But, wait till you hear the quality cf the original cassette recordings and copies you'll make.

Just to test the quality of the copies, take your favorite tape, copy it, and then compare the difference. You'll be amazed at the crisp high quality of the new copy.

A note about Dolby®. If you have a tape recorded with either Dolby B or C, you can copy it on this deck and the copy will still be recorded in perfect Dolby. If you simply play a tape that's been recorded in Dolby, it will sound brighter and more vibrant than normal.

In fact, many people record cassettes in Dolby to play through their car stereos. What's really interesting, is that most car stereos don't have Dolby. But Dolby tapes make high-end starved car stereos sound more vibrantly alive because the highs in the recordings are boosted.

And, speaking of car stereos, this deck provides you with a great way of making duplicate tapes you can play in your car [illegible]use with your personal stereo.

[illegible]ow you can leave your original tapes s[illegible]ely at home, and let the sun, wind, [illegible]d dust 'destroy' only your copies. So, [illegible]ou can both build your music collection and protect it with this new high speed dubbing Portable Cassette Factory.

And, you just may want to test the vibrant sound of a few tapes recorded with Dolby in your car. (Look at it this way, if you don't buy The Factory, you won't have read this ad for nothing.)

BUT IT'S THE MUSIC

Sure, you'll make copies, and sure you'll add to your collection. But most of the time, you'll simply want to hear beautiful music. And look at what you'll get.

First, you'll play beautiful music for a long time. When you push the Continuous Play button, the deck will allow you to listen to the cassette in Deck A, and then automatically switch to the cassette in Deck B for uninterrupted music.

If you're in the great outdoors, just push the Loudness Contour button and you'll hear the low depth of your music increase to fill your listening area.

If you sing, there's mike mixing. Just plug-in your own mike and you can add your voice to any tape you are recording.

You can select your choice of the sensitive AM or FM stereo tuners which really pull in and lock even weak distant stations, Tape, or an Aux inputs. Of course, you'll find all the standard controls including 'pause' on each cassette deck, a digital counter for the record deck, mono/stereo for FM and a headphone jack.

The Portable Cassette Factory is loaded with LED indicators that show virtually every function at a glance. And, with its full range speakers, it sounds as good as it looks. It's made by Emerson, and it's backed by their standard limited warranty.

TRY THE CASSETTE FACTORY
RISK FREE

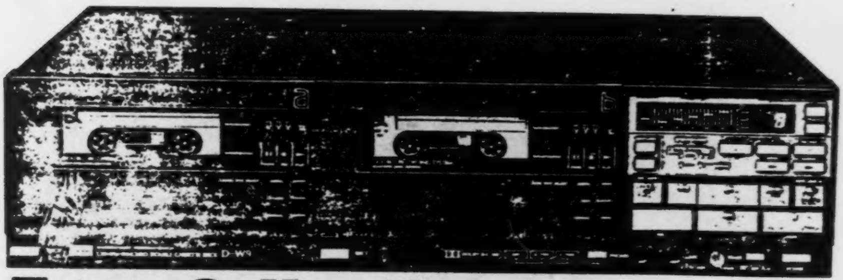
Make some normal recordings when the The Factory arrives. Then take any cassette and duplicate it at normal speed. Finally, try the high speed dubbing.

Listen to the crisp clean quality, not just of your cassettes but of the AM and FM stereo too. If you're not 100% satisfied, simply return it in its original box within 30 days to DAK for a refund.

To order your Emerson High Speed Cassette Dubbing, AM, FM Stereo Portable Cassette Factory risk free with your credit card, call toll free, or send your check for DAK's amazing multi-truckload purchase price of just $99 plus $6 for postage and handling. Order No. 9845. CA res add sales tax. Note: Massive shipments are scheduled to begin July 1.

Increase your tape library with the latest innovation in portable recording equipment. And enjoy great sounding music wherever you are, even at home.

DAK
INDUSTRIES INCORPORATED
TOLL-FREE ORDER LINE
For credit card orders call 24 hours a day 7 days a week
CALL TOLL-FREE. . .1-800-325-0800
10845 Vanowen St., N. Hollywood CA 91605



Tape Collection Expander

Copying tape[illegible]lest thing this dual recording cassette deck with Dolby C, RMPS, and [illegible]quent[illegible]ecord and play [illegible]n do. It's much more than just two recording decks.

You're listening to FM. Suddenly you realize that a song you really like is being played. And unfortunately, you've already daydreamed through half of it.

Well, now you can build yourself a flawlessly recorded cassette collection of only your favorite songs almost effortlessly. Simply set this new relay recording dual cassette deck to record, 'tune-in' your favorite FM station, and leave.

When you return, you'll have one side of each cassette recorded with the music you missed. Then just start listening to the cassette in deck 'A'.

Whenever you hear a song you like, just touch one button and you'll compile a collection of tapes with just the music you like by copying them onto a blank cassette in deck 'B'.

And, wait till you hear the [illegible] that these incredible decks produce. You're getting two true audiophile decks for less than the cost of just one.

A REAL DREAM MACHINE

It's the sound. The frequency response reaches 16,000hz with normal tape, 18,000hz with Chrome and 19,000hz with metal.

The signal to noise ratio is 58db without Dolby, 68db with Dolby B, and 78db with Dolby C. But, look at this. All these specs are for both decks, not just one.

You see, this all new dual cassette dream machine is really two separate cassette decks with 6 motors, and completely separate circuits housed in one dramatic high-tech black cabinet.

Wait till you use this deck. There's only one set of operational controls. You just push the 'A' or 'B' button before you push play, record, fast forward etc. And, if you want, just push the 'AB' button and both decks will spring to life.

To copy a tape, just put the recorded tape in deck 'A' and a blank cassette in deck 'B'. Then just push 'Dub'.

RMPS

And, speaking of automatic, this deck will search up to 15 different selections to find just the song you want. And, you can program it to play up to 3 songs in the order you choose. Of course, you can copy the selected songs as you listen.

SOUND ON SOUND

If you sing, this is the deck for you. Here's what you do. You can play a music tape on deck 'A', plug in a microphone and sing along while you record everything on deck 'B'.

Or, if you're really into professional applications, look at this. Record your own voice on either deck 'A' or 'B'. Then play the tape back in deck 'A' while you sing harmony to your first vocal.

Of course, you'll be recording your 'duet' on deck 'B'. Then take the tape from deck 'B' and put it in deck 'A' and repeat the process. Now you're a trio, then a quartet and finally a chorus.

With the incredible signal to noise ratio of this deck, you can really add on. Of course, you can do simple things like be a disc jockey and add your comments to any tape as it's being made. But singing along is really exciting.

DOUBLE RECORDING

In addition to the relay recording described above, you can make two identical recordings at the same time.

Each deck has a High-Bs hard permalloy head and a double-gap ferrite erase head. Each of the main transport motors is an electronically controlled DC motor for a maximum wow and flutter specification of just 0.04% (WRMS).

Each deck has a separate tape counter and each has automatic bias sensing. You can record Chrome in one deck and normal in the other automatically with no buttons to push. This is a very intelligent tape deck indeed.

And speaking of intelligent, it has a feature that is showing up more and more in high quality decks that I think we 'tape nuts' are just going to have to get used to.

This deck features Automatic Level Control for each deck. It does have a peak reading LED meter, but I think they put it in just to prove to us that it knows what it's doing.

And frankly, it does. You won't notice any of the dynamic range compression that I've always associated with automatic level control.

What you will notice is perfectly recorded tapes every time. I still miss the controls, but I must admit that the recording is flawless.

There is one recording level control. It's for the sound on sound mike recording. So, I guess they still need humans for something.

There's much more. You won't have to worry about where to start recording. Touch the tape 'lead-in' button and the deck will be automatically advanced past the leader.

If you have a timer, like the BSR system described on pages 3 to 5 of this catalog, you can set this deck to play or record when you are at work or asleep.

And, just one look at the control panel is enough to send the average astronaut into 7th heaven. There are mode indicators for virtually every function and audible indicators signal the actions.

The Tape Collection Expander is made by Sansui. It's their top of the line, and it sounds like it is. It is 17" wide, 4½" tall and 12¼" deep. They back it with a standard limited warranty.

EXPAND YOUR TAPE COLLECTION RISK FREE

Record from the most dramatic digital disk you own. Then listen to the tape. You'll be sold. Then copy the tape and listen to the copy. You'll find it hard to believe your ears.

You'll copy a friend's tapes, make fabulous live tapes and make spare tapes for your car and personal stereo. If you aren't 100% satisfied, simply return it to DAK in its original box within 30 days for a courteous refund.

To order your Sansui Tape Collection Expander risk free with your credit card, call toll free or send your check for DAK's breakthrough price of just $349 ($7 P&H) Order Number 9792.

Now you can have great music and total automation. And best of all, along with the audiophile quality, you can easily build a massive, totally personalized, tape collection that you'll enjoy for years.

artists and their biggest hits from the radio and stereo . . . ."[17]

These statements and the survey evidence cited above demonstrate that the home taping that has already reached massive proportions will -- with the active encouragement of the electronics industry -- continue to escalate rapidly. As will next be shown, this home taping results in widespread displacement of record sales and has a profoundly destructive effect on the music community, the listening public and the nation as a whole.

II. HOME TAPING HAS SERIOUS ECONOMIC AND CULTURAL IMPLICATIONS

The impact of home taping is felt not only by the music industry, but by all who love music. By enabling some to get music virtually for free, home taping undermines the economic security of the hundreds of thousands of working people nationwide -- the music publishers, songwriters, musicians, vocalists, manufacturers, distributors, retailers, and suppliers -- who depend upon the music industry for their livelihoods. Widespread home taping also has a negative impact on one of the few American industries with a favorable effect on our international balance of payments -- an industry that, in addition, has generated enormous goodwill around the globe.

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[17] Transcript, Bob Craft on WSAC, Elizabethtown, Kentucky, July 1985.

The damage caused by home taping transcends purely economic consequences, however. Losses resulting from continued massive home taping will cause record companies to release fewer records and to experiment with fewer new artists, songwriters, and types of music. Music publishers, too -- whose royalties are based upon sales -- will no longer be able to cater to as broad a range of tastes as they do today. The result will be a significant decline in the number and variety of records and types of music available to all consumers -- those who buy, as well as those who tape.

A. The Volume of Record Sales Displaced by Home Taping Is Enormous

The Audits & Surveys study calculated the volume of record and prerecorded tape sales displaced by home taping. With respect to each instance in which a respondent made a home tape, he or she was asked: "If you had not been able to record what you recorded from this (source), would you have bought a record or prerecorded tape of it instead?" Audits & Surveys aggregated the responses and found that home taping results in lost sales of records and prerecorded tapes equivalent to nearly 325 million albums annually.[18] This conclusion is consistent with those in earlier studies,[19] which also found that home taping results in massive displacement of record sales.[20] Such displacement should come as no surprise; tapers have long admitted that they engage in home taping to avoid buying records.[21]

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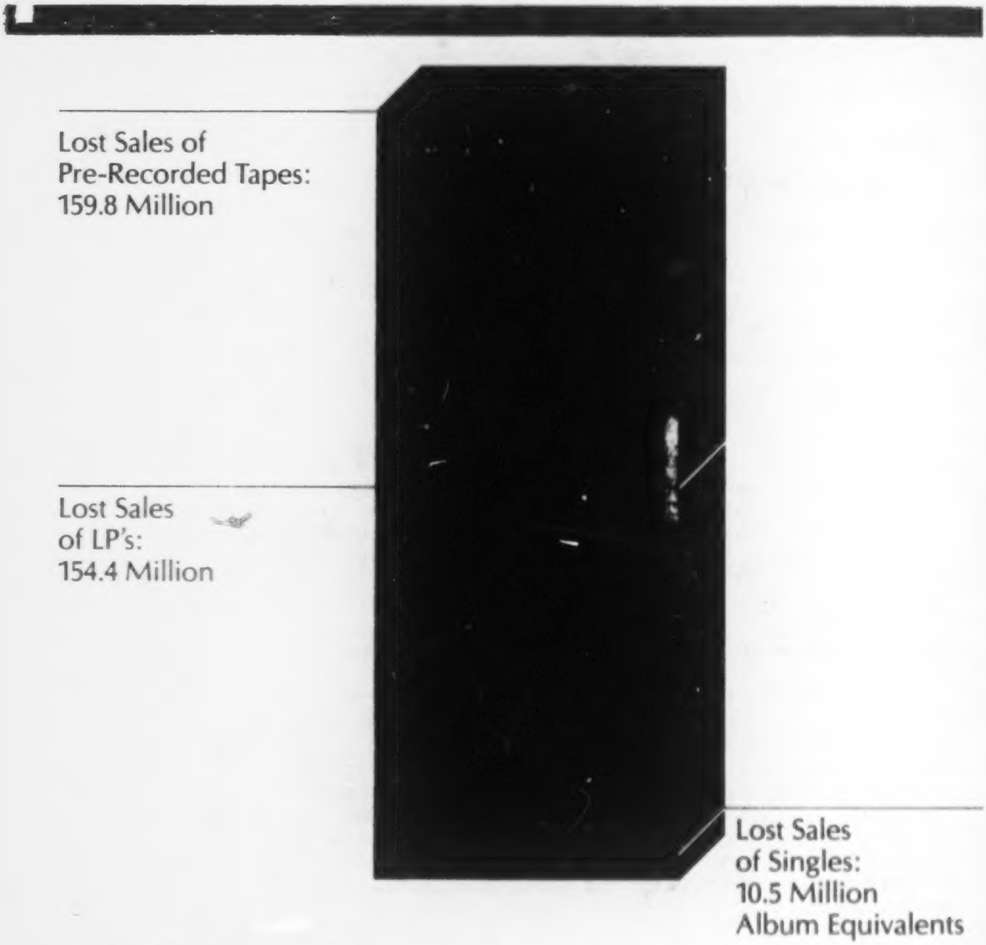
[18] Audits & Surveys Report at 13.

[19] For example, a study conducted by Warner Communications, Inc. found that, for every 10 albums taped, the tapers would have purchased 4 albums if taping were not possible. Warner Communications, Inc., "1981 Estimate of Loss Due to Home Taping: Tapers' Reports of Replacement," at 8 (April 1982). (That study has previously been submitted to this Committee. See 1981-82 Senate Hearings at 938-55.) Similarly, the CBS survey found that home tapers forego three purchases of recordings each year because of home taping. CBS Survey at 14-15.

[20] Because those earlier studies elicited information as to foregone sales with respect to each taper, their displacement figures were unweighted. By contrast, Audits & Surveys asked its displacement questions with respect to each item of music taped; its displacement figure is therefore weighted to reflect each taper's respective amount of taping. This weighted displacement figure more accurately reflects the actual volume of sales lost.

[21] See YSW Report at 21, 84, 92 (69 percent of music tapers identified cost as a reason for preferring home recorded tapes to prerecorded albums; 76 percent identified cost as a reason for preferring home recorded tapes to prerecorded tapes); CBS Survey at 11 (55 percent of blank tape purchasers acknowledged that they taped primarily to save money); WCI Survey at 17 (45 percent of respondents stated that they had taped at least once to avoid purchasing prerecorded music).

Displacement of Sales Caused by Home Taping



Note: 5 singles are equivalent to 1 album.

Source: Interviews of those who taped during diary-keeping period.

B. The Impact of Lost Sales on the Music Industry Is Debilitating

Based upon the survey data, financial statistics of the recording industry, and government and industry data on sales of blank tape and recording equipment, Dr. Alan Greenspan has estimated that in 1984 the recording industry lost about $1.5 billion in sales revenues as a direct result of home taping.[22] This represents a loss of more than one-third of all industry revenues -- $4.4 billion -- for that year.

Dr. Greenspan's analysis is consistent with the dozens of studies in the United States[23] and around the world[24] that have demonstrated that home taping

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[22] Greenspan Statement at 6.

[23] In 1980, WCI found that the actual market value of music taped at home exceeded $2.85 billion, and that the industry lost more than $1 billion in legitimate sales in that year from home taping. WCI Survey at 24; WCI, "1981 Estimate of Loss Due to Home Taping: Tapers' Reports of Replacement," at 8 (April 1982) (35%-40% of home-taped music would have been purchased). The CBS survey estimated that lost sales in 1979 amounted to $700 to $800 million. CBS Survey at 15.

[24] The studies have been undertaken in the following countries:

Australia (Reark Research Pty. Ltd., Taping Survey: A Draft Report Prepared for Australian Record Industry Association (March 1982)).

Austria (Oesterreichisches Gallup Institut, "Tonbandkassetten" (Sept. 1974)).

[Footnote continued on following page]

is responsible for very significant lost sales.

[Footnote 24 continued from preceding page]

Belgium (Belgian Group of IFPA, Market of Recordings on Tapes and Cassettes (1978)).

Britain (Ernst & Whinney for British Phonographic Industry Ltd., Levy on Blank Audio Recording Tape (Draft - Jan. 1982)); British Market Research Bureau Ltd., Home Taping: Report on a Quantitative Survey (Jan. 1980); British Phonographic Industry Ltd., A Levy on Blank Video and Audio Tapes and Associated Hardware (July 1981); British Market Research Bureau Ltd., Home Taping: Report on a Quantitative Survey (Feb. 1982); British Market Research Bureau Ltd., Tape Recording - Report on a Quantitative Survey (Dec. 1973); British Market Research Bureau, Ltd., Tape Recording - Report on a Quantitative Survey (Nov. 1975); British Market Research Bureau Ltd., Tape Recording - Report on a Quantitative Survey (Nov. 1977); Economist Intelligence Unit Ltd., A Study of the UK Market for Blank and Prerecorded Audio Cassettes, Cartridges, and Tapes (1978); Annan Impey Morrish for the British Phonographic Industry Copyright Association, In Home Taping (1978).

Canada (Market Facts of Canada, Ltd., Survey on Purchasers of Blank Tapes: for Canadian Recording Industry Association (April-May 1980); Market Facts of Canada, Ltd., A Report on the Home Taping Practices of Canadians (March 1982); Gallup Poll of Canada, Gallup Audio Equipment Study (April 1980)).

Denmark (Nordic Research Association, Cassette Recording 1977 (Feb. 1977); The Danish Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway, and Denmark (Jan. 1980)).

Finland (The Finnish Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway and Denmark (1980); Gallup, Commissioned by TEOSTO, Gallup Poll of Home Taping (April 1979)).

France (SOFRES, Poll on Home Taping (May 1983); SOFRES, Survey: Recordings on Tapes and Cassettes (April 1976); SACEM, Intellectual Works Protected by Copyright -

[Footnote continued on following page]

The magnitude of the problem is apparent when the losses caused by home taping are compared with the damage inflicted by commercial record piracy. Many

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[Footnote 24 continued from preceding page] Private Copying (March 1979)); Louis Harris - France, The World of Music - Recordings of Discs on Cassettes (May 1980)).

Germany (The German Group of IFPI, et al., Market Research Survey Sponsored by GVL (1982); GFM/Gesellschaft fuer Marktforschung, Recording of Music onto Blank Cassettes (1980); The German Group of IFPI, GVL, Copying of Music onto Blank Cassettes (April 1978)).

Japan (The Japanese Group of IFPI, et al., "Drastic Steps Urged To Save Record Industry," Mainichi Daily News (October 11, 1982); Electronic Association of Japan, Survey on Home Taping (1979); JASRAC, GEIDANKYO, and Japan Phonograph Record Association, Actual Survey on Private Recording (October 1976)).

Netherlands (Netherlands Association for the Phonographic Industry (NVPI), Home Taping: Investigation into the Making of Sound Copies on Tape and Cassettes by Individuals in the Netherlands in 1979 (Sept. 1980); SEO for STEMRA and NVPI, Survey on Private Copying (June 1976)).

New Zealand (Heylen Research Centre for the New Zealand Federation of the Phonographic Industry, Personal Tape Recording - A Study in Blank Tape Usage (Nov. 1976)).

Norway (Nordic Research Association, Cassette Recording 1977 (Feb. 1977); The Norwegian Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway, and Denmark (Jan. 1980)).

Sweden (Nordic Research Association, Cassette Recording 1977 (Feb. 1977); The Swedish Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway, and Denmark (Jan. 1980)).

people assume that commercial piracy -- in which millions of illicit copies of popular recordings are manufactured for resale to the public -- is the most serious form of unauthorized copying faced by the music industry today. In fact, the aggregate impact of the actions of the millions of individuals who engage in home taping just for private use is far greater. Home taping is responsible for more lost sales in the United States alone than record piracy is worldwide.[28]

By any measure, therefore, the damage home taping causes to the music community has reached staggering levels, and the repercussions for the music community are enormous. Home taping reduces the sales revenues that are record makers' only source of compensation, and the primary source of income for all others in the music industry. It reduces royalties for songwriters, lyricists, recording artists, musicians, vocalists and their unions. And it cuts into the revenues of record retailers, distributors, rack jobbers, manufacturers, pressers, printers and suppliers of every kind -- the hundreds of thousands of working people across the country who depend on sales of prerecorded music for their livelihood. Between 1978 and 1984, for example, total employment in the recording industry fell by 34 percent.[26] Moreover, wages paid to union musicians by recording companies in 1983 -- $22,346,[illegible] -- were more than 17.5 percent lower than wages paid in 1982 ($27,111,870). This was the sixth consecutive year in which wages declined.[27]

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[28] As noted above, home taping in the United States displaced about $1.5 billion in revenue in 1984 alone; in contrast, the annual worldwide impact of record piracy is about $1.2 billion. See "Extent of Piracy of Sound Recordings Worldwide in 1984," International Federation of Phonograph and Videogram Producers, June 1985.

But this is not the only damage caused by home taping. Record companies have had to reduce facilities, consolidate operations, slash their artist rosters, and sharply limit their signing and promotion of new talent. They have also released fewer albums -- according to RIAA statistics, 48 percent fewer LPs were released in 1984 than in 1978.[28] Music publishers, too, have had to cut back on experimentation and innovation. The impact of this retrenchment has been felt directly by all who enjoy music, and indeed by the public as a whole.

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[26] Greenspan Statement, Table 7.

[27] Billboard, July 21, 1984 at 1.

[28] Recording Industry Association of America Press Release, March 27, 1985 at 2.

C. The Consequences for the Listening Public Are Severe

Everyone who enjoys music is hurt by home taping. Home taping is a perfect example of why economists say that "there's no such thing as a free lunch." Tapers may get music virtually for free, but the public as a whole pays the price for it.

The cost of an album includes much more than the cost of manufacturing the vinyl disk or the tape cassette. That album is merely the physical medium embodying valuable intellectual property; as with virtually all mass-market intellectual property, it is only through selling the physical medium that the costs associated with creating and producing the intellectual property itself can be recouped.

Home taping allows one group of music consumers -- those who tape -- to avoid paying their share of these costs. The costs of creating and producing music are shifted entirely onto another group of music consumers -- those who purchase copyrighted material -- or, more likely, they are absorbed by composers, performers, and others who work in the music industry as well as by publishers, record companies and their shareholders. In economic terms, home tapers are enjoying a "free ride" at somebody else's expense.

Regardless of who foots the bill in the first instance, the "free ride" for home tapers encouraged by the tape and equipment manufacturers ultimately imposes very real burdens on all consumers and the listening public, including home tapers themselves:

First, home taping means less investment in new music. It siphons off revenues that otherwise would be spent on new music. That's one of the reasons why the number of new albums released has plummeted by almost half since 1978[29] and why record companies and publishers are less willing to experiment with new artists, new songwriters and new types of music.

Second, home taping means reduced support for more specialized forms of music. Jazz, classical, folk, gospel and ethnic records rarely turn a profit; they are heavily subsidized by the profits from big hits.[30] Home taping dries up the funds record companies use to produce important music that nevertheless lacks mass appeal.

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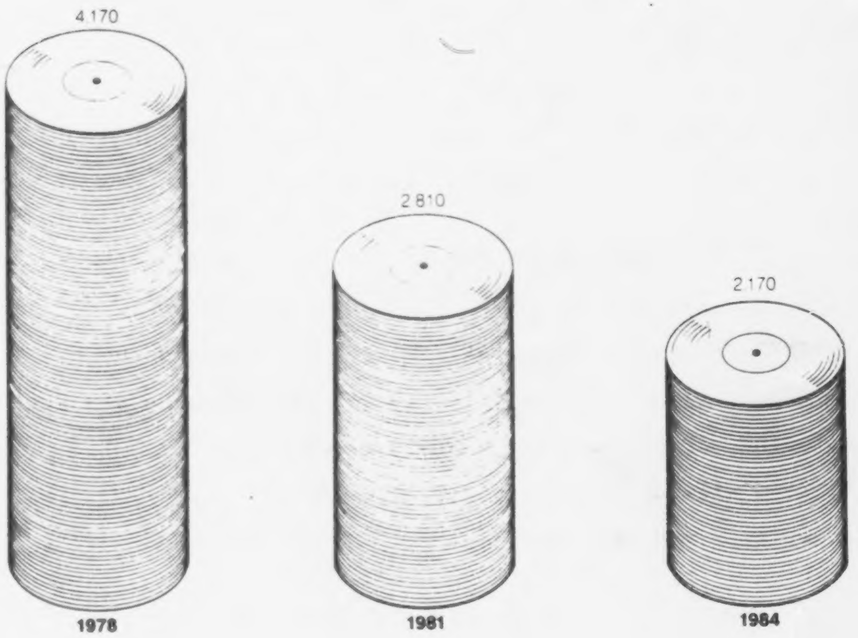
[29] Recording Industry Association of America Press Release, March 27, 1985 at 2.

[30] Home Recording of Copyrighted Works: Hearings Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary, 97th Cong., 2d Sess. 547 (1983) (Testimony of Jerry Moss).

Over the last six years, the number of new albums released has dropped by nearly half. This means that less new music is available each year.



Third, home taping can mean more expensive music. By reducing sales volume, home taping can force record companies to spread their costs of production over fewer albums. The result would be higher prices for the records that are sold. Thus, those who buy records would pay more so that those who tape can pay nothing.[11]

Finally, home taping means, quite simply, less music for the public. Home taping undermines the fundamental premise of our copyright system -- that compensation for the use of intellectual property is a necessary incentive for its creation. By denying to copyright owners compensation for the use of their property, home taping diminishes the incentive to invest time, effort and money in the high-risk music industry, and ultimately decreases the amount of music that will be produced for any consumer to enjoy.

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[11] This Committee has explicitly identified these consequences of displaced sales. In considering the "Record Rental Amendment of 1983," this Committee indicated its concern that sales displacement would cause (1) increased record prices that would unfairly "forc[e] legitimate purchasers to subsidize those who tape rented records"; and (2) "record companies and music publishers [to] become less willing to take a chance on unknown artists and songwriters or to experiment with innovative musical forms." In each case, the Committee recognized that "the consumer is the ultimate loser." S. Rep. No. 98-162, 98th Cong., 1st Sess. at 3 (1983).

D. Home Taping Adversely Affects the Nation's Economy

The losses caused by home taping also adversely affect the nation as a whole. This is because home taping has a negative impact on the nation's balance of trade, an impact that is particularly significant in this time of rising budget deficits and worldwide concern about the strength of the dollar and the prospects for the United States economy.

American music is the most sought-after music in the international marketplace, and the music industry has long been one of the few American industries that has had a positive effect on our trade balance. The value of American exports of phonorecords has been about three times as great as the value of our imports.[11] The royalties we receive from foreign countries for public performances of copyrighted music have been many times greater than the payments we make to copyright owners abroad. Similarly, license fees paid to American publishing and recording companies by foreign manufacturers and licensees have vastly exceeded the license fees flowing out of the United States.

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[11] See, e.g., "U.S. Trade Shifts in Selected Commodity Areas," U.S. International Trade Commission Publication No. 1405 (First Quarter 1983).

Home taping around the world has two negative consequences for our international balance of payments. First, displaced sales reduce revenue flowing into the United States from abroad. Second, because home taping leaves the music industry with less revenue to invest in new musical recordings, it reduces the number of products the United States has available for export. In 1984, for example, the industry released many fewer albums than it had in 1978.[33] That means there were many fewer export products, a situation which only further undermined America's position in the international marketplace.

By contrast, foreign manufacturers have profited handsomely by home taping. Most taping equipment and blank tapes bought in the United States are imported (principally from Japan) or produced by foreign-controlled interests -- and those interests have been riding the crest of the home taping wave. The value of blank audio tape imported into the United States in 1984 ($710,016,000) was more than three times the value of the tape imported in 1980 ($229,597,000). Similarly, the value of tape recorders imported into the United

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[33] Recording Industry Association of America Press Release, March 27, 1985, at 2.

States tripled between 1980 and 1984, rising from $1.6 billion to $5.3 billion.[14] These advances have been made at direct cost to American industry and to the American economy; in effect, the manufacturers and importers of tapes and taping equipment have found a way to divert billions of dollars from copyright owners to themselves.

Thus, from any perspective -- that of the music community, record buyers, the listening public, or the nation as a whole -- home taping has already had negative effects. The harm it causes will continue to grow unless Congress acts.

III. A LEGISLATIVE SOLUTION IS REQUIRED

The serious harm caused by home taping and documented above demonstrates that it is in the best interests of consumers and the music community alike to find a solution to this ever growing problem. The music community's past efforts prove that there is no effective alternative to a legislative solution. Moreover, such a legislative solution is emerging as the international norm.

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[14] U.S. Department of Commerce, Annual Data on U.S. Imports and Exports for Selected Commodities Groups, 1980-1984.

A. The Music Community Has No Realistic Alternative

Despite the growing proportions of the home taping phenomenon, the music community has no realistic or effective way to combat the problem or to avert its consequences in the absence of legislation. There is simply no other way in which it can curb the damage done by home taping.

First, as Dr. Greenspan has noted, there is no pricing strategy that record companies can adopt to combat home taping. If the recording industry attempted to raise prices in an effort to recoup losses, it would only further reduce the sales of prerecorded music and increase the shift toward lower-cost home taping -- as well as unfairly penalize those who continue to buy their music instead of taping it. If, alternatively, the record companies cut prices to narrow the gap between home taping costs and retail record prices, they would decrease their capability to take the type of risks that the nature of the record business requires.[35]

Second, there is no technological solution to the home taping problem that can be implemented by the music community alone. Techniques are available by which records and tapes can be encoded with a signal that can control home taping. But this solution cannot be implemented without the cooperation of the Japanese recording equipment manufacturers, who would have to include a decoding device in their machines.[38] They have steadfastly refused even to discuss such a solution with the American music community. This is unfortunate, because an encode/decode system offers a true marketplace solution to the home taping problem. Buyers could decide whether or not to purchase, and how much to pay for, recordings encoded so that they are capable of being taped.

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[35] Greenspan Statement at 9-10.

Third, there is no marketing solution to the home taping problem. Home taping has grown in spite of the continuing efforts of record companies to make prerecorded music cassettes more attractive. The companies have tried including extra tunes on prerecorded cassettes; improving the quality of those tapes; including lyrics in cassette packages; offering incentives -- *e.g.*, free posters and booklets -- to cassette purchasers;

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[38] The Home Audio Recording Act includes an exemption from the proposed equipment royalty for machines that contain encoder/decoder devices. See § 119(d)(2) and discussion infra. This exemption provides an incentive for equipment manufacturers to include such a device in their machines.

selling cassettes recorded with a different album on each side; and warning the public that unauthorized duplication of copyrighted material is illegal. None of these efforts has made even a dent in the huge and growing volume of home taping.

Finally,[37] there can be no negotiated solution to the home taping problem. The American record industry has tried repeatedly to work out a solution with the Japanese manufacturers of tape and equipment -- but every overture has been rejected. Those manufacturers refuse even to meet with music representatives to discuss home taping. At the same time, news publications report that "the Japanese plan to fund opposition efforts to home taping legislation -- until the dawn of the next decade if necessary" and that "they will accept no compromise from the Congress."[38] This arrogant attitude has forced the American music community to conclude that voluntary negotiations will not solve the home taping problem. Legislation is necessary to save America's music.

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[37] As will be discussed in greater detail infra, there is also no legal solution, short of legislation, that the music community can pursue. Although, as a legal matter, the music community believes that audio home taping constitutes copyright infringement, it is obviously impractical and undesirable to sue home tapers. The music community's legal rights are thus, for all intents and purposes, unenforceable.

[38] "Manufacturers Ready for Copyright Battle," Billboard, January 5, 1985.

B. A Legislative Solution Is Emerging as the International Norm

The United States Congress will not be breaking new ground by enacting a legislative solution to the home taping problem. To the contrary, a legislative solution -- and in particular a royalty on blank audio tapes and audio recording equipment -- has become the standard international solution to the worldwide problem of home taping.

At least ten other countries -- Austria, the Congo, Finland, France, Hungary, Iceland, Norway, Sweden, Turkey, and West Germany -- have already enacted legislation under which royalties on blank audio tape or audio recording equipment are distributed to copyright owners as remuneration for unauthorized home taping.

Similar legislation is pending or being drafted in an additional twelve countries -- Australia, Belgium, Brazil, Canada, Czechoslovakia, Italy, Japan, the Netherlands, Portugal, Spain, Switzerland and the United Kingdom. Only recently, for example, the Government of the United Kingdom issued a "Green Paper" proposing that a royalty be added to the sale of blank audio tapes;[39] a subcommittee of Canada's House of Commons similarly recommended adoption of a royalty system on blank tapes and taping equipment to compensate copyright owners for losses resulting from home taping.[40]

All of these countries have recognized that a legislative solution is required to solve the home taping problem. The United States -- the acknowledged leader in producing and exporting music to the rest of the world -- should not fall behind other major countries in protecting music creators.

Indeed, Congress has itself recognized on numerous occasions that U.S. leadership in the information age -- a time in which the power of ideas is the key to American economic growth -- demands creative action to protect all forms of intellectual property. For example, recently Congress extended new intellectual property protection to computer chips,[41] closed a loophole that allowed record rental shops to escape royalty payments to music creators,[42] increased the penalties for counterfeiting of trademarks,[43] and conditioned trade benefits to developing nations on their willingness to respect intellectual property rights.[44] To maintain its position in the forefront of intellectual property protection, Congress must now enact home taping legislation.

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[39] "The Recording and Rental of Audio and Video Copyright Material," Secretary of State for Trade and Industry, February 1985.

[40] "A Charter of Rights for Creators," Report of the Sub-Committee on the Revision of Copyright of the Standing Committee on Communications and Culture, House of Commons at 73-77 (October 1985).

[41] Pub. L. No. 98-620, November 8, 1984.

C. Legal Principles Mandate Compensation for Audio Home Taping

The legal principles underlying our copyright system mandate that compensation be paid for audio home taping. The Supreme Court's decision in the "Betamax"[45] case is consistent with this requirement.

In Betamax, the Supreme Court decided that the sale of video recording equipment does not constitute a contributory copyright infringement. That ruling was predicated on two crucial factors: first, that the primary use of VCRs is to "time shift" television programs, and second, that such time shifting is a fair use because the plaintiffs in that case did not demonstrate that it results in harm to the actual or potential market for, or value of, the copyrighted works taped.

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[42] Pub. L. No. 98-450, October 4, 1984.

[43] Pub. L. No. 98-473, October 12, 1984.

[44] Pub. L. No. 98-573, October 30, 1984.

[45] Sony Corp. of America v. Universal Studios, Inc., 104 S. Ct. 774 (1984).

The Supreme Court did not reach the issue of the legality of *audio* home taping, and very carefully limited its ruling to the context of time-shifting of video works -- taping television programs to see them once at a later time.

Audio home taping presents quite different issues, of course. There is no time shifting in audio taping; people don't tape records to listen to them once. In addition, as surveys and reports have repeatedly demonstrated, the music industry is losing massive amounts in sales revenues to home taping -- a cost that amounted to about $1.5 billion in 1984 alone. The industry can thus show precisely the kind of harm the Court stated was necessary in the *Betamax* case.

As a legal matter, there can be little doubt that audio home taping constitutes copyright infringement.[46] Home taping deprives copyright owners of their exclusive right to "reproduce the[ir] copyrighted work in copies or phonorecords." 17 U.S.C § 106 (1976). Uncompensated home taping also deprives creators of music of a just reward for the use of their works -- a reward which is central to the constitutionally established copyright scheme that ensures compensation to creators so as to encourage the further production of literary and artistic work for the public benefit.

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[46] *See*, *e.g.*, Nimmer, *Copyright Liability for Audio Home Recording: Dispelling the Betamax Myth*, 68 Va. L. Rev. 1505, 1506 (1982); *Home Recording of Copyrighted Works: Hearings Before the Subcomm. on Courts, Civil Liberties and the Administration of Justice of the House Comm. on the Judiciary*, 97th Cong., 2d Sess. 528-44 (1982) (testimony of Jon Baumgarten).

But the fact that home tapers are violating the copyright law does not help the music industry as a practical matter. It is obviously impractical and undesirable to sue home tapers, and the legal rights that music copyright owners have are meaningless without an effective remedy. Thus, only Congress can devise a solution -- by crafting legislation that permits home taping but also enables creators to be compensated for their work.

The Supreme Court itself recognized this fact. The Betamax decision was narrowly decided by a 5-4 vote. But there was one point on which all nine Justices were unanimous -- that Congress should resolve the problems posed by new home taping technology. As Justice Stevens, writing for the majority, noted:

> Congress has the constitutional authority and the institutional ability to accommodate fully the varied permutations of competing interests that are inevitably implicated by such new technology.[47]

For the minority, Justice Blackmun likewise expressed the hope that "these questions ultimately will be considered seriously and in depth by the Congress and be resolved there. . . ."[48] The Home Audio Recording Act is Congress' response to the Court's invitation in the audio taping context.

IV. THE HOME AUDIO RECORDING ACT PROVIDES A WORKABLE LEGISLATIVE SOLUTION TO THE HOME TAPING PROBLEM

The Senate now has before it legislation that will provide a fair and workable solution to the home taping crisis: the Home Audio Recording Act (S. 1739). This bill embodies the two basic principles that are essential to any solution of the home taping problem:

- -- Consumers who tape copyrighted works in their homes for private, non-commercial use should not be liable for copyright infringement.
- -- Those whose works are being taped should be compensated by means of a royalty on the sale of recording equipment and blank tapes.

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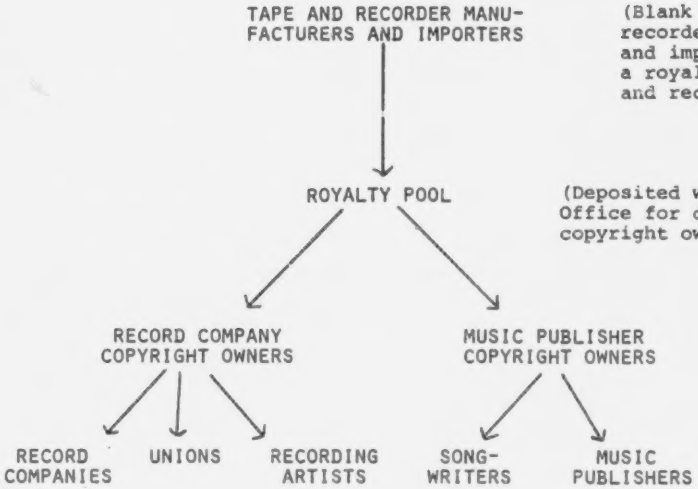
[47] 104 S. Ct. at 783.

[48] _Id_. at 796.

The Act draws upon previous home taping legislation, but it differs from those efforts in several notable respects. First, the Act addresses only audio -- and not video -- home taping. Second, it fashions new protections for those who tape noncopyrighted material. Third, it specifies the amount of the royalty on both blank tapes and recording equipment. The specific provisions of the bill are described in greater detail below.

A. Compulsory License

The Home Audio Recording Act establishes a royalty system (technically called a "compulsory license") to compensate copyright owners whose musical works or sound recordings are taped. As the chart on page 50 demonstrates, the compulsory license mechanism works fairly simply. In essence, manufacturers and importers of blank audio tapes and taping equipment pay a one-time royalty per unit when they first sell or distribute their products in the United States. The proceeds of that royalty are collected by the Register of Copyrights for distribution to the music copyright owners and creators harmed by home taping.


TAPE AND RECORDER MANUFACTURERS AND IMPORTERS
ROYALTY POOL
RECORD COMPANY COPYRIGHT OWNERS
MUSIC PUBLISHER COPYRIGHT OWNERS
RECORD COMPANIES
UNIONS
RECORDING ARTISTS
SONGWRITERS
MUSIC PUBLISHERS

(Blank tape and tape recorder manufacturers and importers would pay a royalty for each tape and recorder they sell.)

(Deposited with the Copyright Office for distribution to copyright owners.)

(Copyright owners share the royalties, by contract, with others responsible for creating and producing their works.)

The Act provides that the compulsory license applies to: (i) blank tape capable of recording music in any format commonly sold for private use (*e.g.*, blank cassettes); (ii) standard recording equipment which can be used for home taping, and which is capable of recording music by internal or external wiring from a radio, television or record player; and (iii) dual cassette recorders. The compulsory license does *not* apply to "multiple audio recording devices" (cassette recorders with three or more wells) because the purpose of such machines is so clearly to facilitate large-scale infringement that they promote activity more akin to commercial piracy than to copying for personal use. The Act thus makes it an act of infringement to distribute these machines in the United States.[49]

B. The Royalty Rates

The Act establishes three different royalty rates. First, it sets a royalty on blank cassette tape of one cent per minute of playing time.[50] The royalty on audio recording equipment is set at 5 percent of the wholesale price of the equipment.[51] Producers of dual cassette recorders -- machines that, as noted above, are designed specifically to facilitate the copying of prerecorded music -- pay a special, higher royalty of 25 percent of the wholesale price.[52] These rates may be adjusted by the Copyright Royalty Tribunal every five years, based on ten specified criteria.[53]

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[49] Section 119(b)(2)(B).

[50] Section 119(c)(1)(C).

These proposed royalty rates are reasonable; the price of home taping an album will continue to be a mere fraction of the value -- and cost -- of that album. The royalty to be imposed on the sale of blank tapes -- one cent per minute of playing time -- is a good illustration. Even if the entire royalty were passed on to the consumer by the manufacturer (which is unlikely due to competitive factors),[54] the royalty on a 90-minute tape -- which can capture two full albums -- would cost 45 cents per album (compared with a retail album cost of about $6.80). Since albums generally contain about 10 tunes, the cost would be only 4-1/2 cents per song. And tapers would only pay once, even though a cassette can be used to tape other recordings dozens of times. If that tape were reused just one time, the royalty would drop to just 2-1/4 cents per tune. That is a modest sum to be shared by the songwriters, music publishers, record companies, performers, musicians, vocalists and unions represented on any one song.

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[51] Section 119(c)(1)(A).

[52] Section 119(c)(1)(B).

[53] These criteria include the projected impact of the fees on consumers and on the electronics industries; the level of royalties necessary to maximize the creation of new music; the extent to which tapes and recording equipment have been used for noninfringing purposes; the amount of compensation of which home taping has deprived copyright owners; the value to an individual of the right to tape music; the benefits derived by the electronics industries from the distribution of their products; the relative roles of copyright owners and manufacturers and importers with respect to the creative and technological development of music; and the existence of new technologies for making audio recordings. Section 119(c)(2)(B).

As is obvious from this example, the amount generated by the compulsory license will not even come close to making creators and copyright owners whole for the losses they incur due to home taping. Certainly, not all of the $1.5 billion lost in sales revenues are actual losses to the music community. For example, record companies do not incur the costs of manufacturing or distributing the records and prerecorded tapes whose sales are displaced by home taping. The net loss actually sustained, according to Dr. Greenspan, is approximately two-fifths of the music industry's retail losses -- or some $600 million.[55] The proposed royalties in S. 1739, however, would yield only about $200 million annually[56] -- about one-third of the actual loss. If anything, therefore, the royalty rates are lower than they should be if music creators and copyright owners are to be fully compensated for the damage inflicted by home taping.

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[54] See discussion at p. 57, infra.

C. Exemptions

The Act gives the Copyright Royalty Tribunal authority in two specific cases to exempt from royalty fees particular kinds of recording equipment or blank tapes that are used for noninfringing purposes.

First, the Tribunal may exempt equipment or tape found to be "unsuitable" for home taping of recorded music on the basis of "technical criteria" such as reproductive quality.[57] Under this authority, for example, the Tribunal may exempt business dictation machines and microcassette tapes.

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[55] Greenspan Statement at 12.

[56] Id.

[57] Section 119(c)(1)(D).

Second, the Tribunal may exempt equipment or tape that is used in a trade or business or for professional purposes, and not for personal taping of recorded music.[58] The exemption includes purchases by profit-making entities (such as commercial radio stations) and by nonprofit entities (such as National Public Radio). In both instances, however, the use of the purchased equipment or tape must be noninfringing: this provision does not authorize the purchase of royalty-free equipment or tape by a commercial pirate.[59]

The Tribunal is to develop procedures for the administration of this exemption. Presumably, purchasers will be asked to certify that they meet the two-pronged test set forth in the statute: that their purchases are deductible "as an ordinary and necessary business expense under Section 162 of the Internal Revenue Code . . . or as an allowance for depreciation under section 167 of such Code";[60] and that the tape and equipment will be used for noninfringing purposes. Qualified purchasers will likely secure royalty-exempt tape and equipment directly from the manufacturers or through specially-placed orders with retailers.

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[58] Section 119(c)(1)(E).

[59] Section 119(c)(1)(E)(ii).

[60] A nonprofit organization wishing to purchase royalty-free tape or equipment will be asked to certify that its purchases would be tax deductible if these Internal Revenue Code sections applied to it.

In addition to these exemptions, the Act excludes from the definition of the devices to which the royalty applies certain types of equipment. Thus, microphone-only recorders and playback-only devices are not subject to the royalty. In addition, S. 1739 specifically exempts those recorders that are equipped with a decoder that controls copying in accordance with instructions encoded in prerecorded records or tapes.[61] By making such equipment royalty-free, the Act provides manufacturers and importers with an economic incentive to equip their hardware with a decoder chip. By this means, the legislation would allow the workings of the marketplace to evaluate the right to reproduce copyrighted works, without any governmental involvement: the marketplace price would vary depending on whether or not the record could be copied.

D. Collection and Deposit of the Royalties

Importers and manufacturers of tapes and taping equipment are required by the bill to file a notice and statement of account, and to deposit fees, with the Register of Copyrights.[62] It is appropriate that the obligation be imposed on these manufacturers and importers of tapes and taping equipment because it is they who benefit most directly from the use of their products for the home taping of music. It is appropriate that both tape and equipment bear a royalty, furthermore, so that royalty payments can be spread across as many units as possible. That way, meaningful sums can be collected while royalty fees can be kept as low as possible. If royalties were to be paid on blank tapes only, the higher fee required would place a disproportionate burden on blank tape sales.

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[61] Section 119(d)(2).

The provision also makes administrative sense: the royalty-collection mechanism is more easily administered among 150 tape and equipment manufacturers and importers than among tens of thousands of retail outlets throughout the United States. In addition, the provision means that consumers may not pay the full amount of the royalty. Competitive factors in the marketplace may, for instance, lead importers and manufacturers to absorb the royalty -- or some portion of it -- as a cost of doing business, rather than passing it through to their customers.

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[62] Section 119(b)(1)(A), (B).

Importers and manufacturers who materially fail to comply with the compulsory license are subject to copyright infringement liability for the distribution of their products.[63] In any infringement action, a court may deprive the importer or manufacturer of its compulsory license for up to 90 days.

E. Distribution of the Royalties

Under the Act, copyright owners are entitled to a share of the royalty fees if their musical works or sound recordings were played on the radio, broadcast on television, or sold in the form of a record or prerecorded tape during the year for which the royalties are collected.[64] Claims for a share of the fees are filed with the Copyright Royalty Tribunal annually.[65]

The legislation obligates all those who have filed claims (or their chosen representatives) to negotiate in good faith among themselves in an effort to reach a voluntary agreement on the distribution of the royalty fees. If the Tribunal determines that there is no controversy concerning the distribution, then the reasonable costs of administering the royalty are deducted from the royalty pool and the royalties are distributed based on the claims filed by the copyright owners.

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[63] Section 119(b)(2)(A).

[64] Section 119(b)(4).

[65] Section 119(b)(5)(A).

If there is a disagreement among any of the copyright owners about the distribution of royalties, then the Tribunal conducts an evidentiary proceeding to determine the apportionment of the royalties. All interested parties would have the opportunity to present their views to the Tribunal. In the meantime, the Tribunal could distribute any uncontested royalty fees, so long as it withheld an amount sufficient to satisfy all the claims still in controversy.[66]

Any administrative costs incurred by the Tribunal in determining the fair distribution of royalties are deducted from the royalty pool.[67] Thus, the distribution mechanism of the Home Audio Recording Act imposes no additional costs on taxpayers.

The Tribunal is only responsible for the first level of royalty distribution -- to the owners of the two copyrights encompassed in every recorded tune, the musical composition and the sound recording. Royalty distributions are to be made to all copyright owners of musical compositions and sound recordings that were included in radio or television programs or distributed to the public in the form of records, prerecorded tapes, or other means during the relevant period.

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[66] Section 119(b)(5)(B).

[67] Section 119(b)(5)(B).

The royalties paid to these copyright owners will, in turn, be shared with all the others responsible for creating and producing the music on the basis of negotiated contractual agreements. Thus, royalties will flow from music publishers to composers and lyricists and from record companies to recording artists, and musicians' and performers' unions.

Industry data bases currently exist or may be readily assembled to provide formulae for the royalty distribution to copyright owners under the proposed legislation. The performance rights societies -- such as ASCAP and BMI -- have the relevant information for radio and television performances of musical works on a current basis. These data are used by them in the distribution of performance royalties to composers, authors and publishers.

A similar data base is available for television transmissions (already in use in cable television royalty proceedings before the Copyright Royalty Tribunal). Mechanical rights licensing organizations -- like The Harry Fox Agency, which licenses mechanical recording rights on behalf of publishers to record companies and collects and distributes the royalties paid by record companies to the publishers for sharing with the composers and authors -- and the record companies themselves have ample data on a current basis on the sale of records and prerecorded tapes.

Home taping royalty distribution systems are also in place in other countries throughout the world where royalty legislation has already been enacted. Even more significantly, the Copyright Royalty Tribunal itself has almost identical responsibilities under current law for overseeing the distribution of royalties to copyright owners of works performed on jukeboxes and cable television systems.[68] Thus, the Tribunal has considerable expertise in the conduct of formal proceedings for royalty distribution purposes. And as previously indicated, all administrative costs incurred by the Tribunal in determining the fair distribution of royalties are deducted from the royalty pool, so that the distribution of royalties under the Home Audio Recording Act imposes no additional costs on taxpayers.

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[68] 17 U.S.C. §§ 111(d), 116(c).

V. THE OBJECTIONS TO THE HOME AUDIO RECORDING ACT ARE WITHOUT MERIT

Opponents of the Home Audio Recording Act -- largely the importers and foreign manufacturers of blank tape and taping equipment -- have concocted numerous arguments in an effort to camouflage the inherent unfairness of their position. Ignoring their own burgeoning sales and profits, they say that the music community is selling enough records as it is, so that Congress need not compensate the industry for the sales it is losing to home taping. Ignoring the demonstrated fact that the overwhelming majority of tape buyers use their tapes to copy music without paying for it, they worry that someone who does not tape music will unfairly pay a royalty. Ignoring their own marketing programs which extol the special virtues of their tape brands for home music recording (see advertisements reprinted on pages 12-17), they caution that it is technically difficult to distinguish music-quality from speech-quality tape. And ignoring the obvious damage that they are inflicting on the American music community, music buyers and music listeners, they assert that the royalty system would be difficult and costly to administer fairly.

Their arguments must be seen for what they are -- justifications to avoid having to pay for the damage their products are causing. They are utterly specious and should be rejected.

A. "The Proposed Royalty Is Unnecessary"

Opponents of the Act claim that the proposed royalty is unnecessary because record sales have improved of late. In fact, according to the Audio Recording Rights Coalition (the "ARRC"), "the recording industry is having its best years ever."[69] From this, opponents conclude that the creation and dissemination of music is not being hurt by home taping, and that a royalty is therefore unnecessary.

This argument is at once deceptive and irrelevant. By its clever use of words, the ARRC would have Congress believe that the recording industry is having "its best years ever" in profits. In fact, the record industry's data lead it to quite the opposite conclusion. According to an analysis by Dr. Alan Greenspan, although sales have improved, profits in the industry remain depressed. He concludes that the impact of home taping on the industry is as evident today as it was in the industry's worst period in the early 1980's.[70] Even the much-noted improvement in record sales is exaggerated. According to RIAA shipment figures, the "rebound" in 1984 did no more than bring the industry up to levels it had long ago achieved in 1978, and the first six months of 1985 already reveal a decline from 1984 levels.[71] And if RIAA's 1984 revenue figures are measured against 1978 figures in constant dollars, revenues for the industry last year were far below prior levels.

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[69] ARRC, "Taxing Blank Tape and Recorders: Untimely, Unnecessary, and Unfair" at 3 (July 1985) (hereinafter "ARRC Pamphlet").

In any event, the ARRC looks to the wrong standard to determine whether the purpose of copyright -- the promotion of additional creation and dissemination of artistic works -- is being served. The ARRC measures the level of artistic creativity and dissemination today "by sales of recordings. . . ."[72] This is the wrong measure.[73]

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[70] Greenspan Statement at 7-8.

[71] Recording Industry Association of America Press Release, October 28, 1985.

[72] ARRC Pamphlet at 2.

[73] If only one new record album were produced each year, it would certainly sell in very great quantities -- probably at a handsome profit -- if only because nothing else was available. The success of that release, however, would hardly establish that the level of musical creation was adequate.

The proper test is not how many copies of a single album are sold, but how many different albums are available for sale. And measured by that standard, the adverse impact of home taping is clear: as RIAA statistics show,[74] the number of new albums released has declined by nearly 50% since 1978.

This result was predictable. The music business is exceedingly risky. According to RIAA industry studies, five out of every six releases fail even to cover their costs.[75] Record companies and music publishers depend on the revenues from the few successful releases to compensate for the failures, and to fund investments in the music of tomorrow -- new artists, new music, new choices from which the public can choose tomorrow's stars.

As home taping drains away the billions of dollars of revenues that could be used for these purposes, it eats away at the industry's ability to create and disseminate new music. The ARRC acknowledges that recording opportunities in the industry have shrunk, that the industry now focuses "its resources on fewer artists" and has stopped "signing contracts with a large number of artists and performers. . . ."[76]

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[74] Recording Industry Association of America Press Release, March 27, 1985 at 2.

[75] Economic Study of the Recording Industry, prepared by the Cambridge Research Institute at 9 (April 7, 1980).

But the ARRC applauds these developments. We, on the other hand, regret them. This industry retrenchment -- forced on it by the increasingly debilitating impact of unrestrained and uncompensated home taping -- means lost opportunities for new recording artists, musicians, and songwriters; less new music; and reduced musical choice for the American public.

The continuing growth of home taping, the depressed profits of the recording industry, and the enormous decline in new releases are hardly coincidental. If the purpose of copyright is to be served, and additional creation and dissemination of music are to be encouraged, home taping royalty legislation is very necessary indeed.

B. "The Proposed Royalty Will 'Tax' Noninfringing Uses"

One of the central arguments advanced by opponents of the Home Audio Recording Act is that the proposed royalty will unfairly "tax" noninfringing uses -- *i.e.*, the copying of things other than copyrighted music.[77] Opponents cite as the underlying premise of this argument surveys that they claim demonstrate that more than half of all home taping does not involve prerecorded music.[78]

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[76] ARRC pamphlet at 8.

This claim is again deceptive. Although some amount of taping may involve noninfringing uses, the relevant question is how many tapes are used exclusively for such purposes. Audits & Surveys found -- after an actual physical audit of tapers' libraries -- that at least 84 percent of home tapes are used to record music.[79] This is a minimum figure because it did not count either tapes that were used to record music and were then erased, or those that will be used for taping

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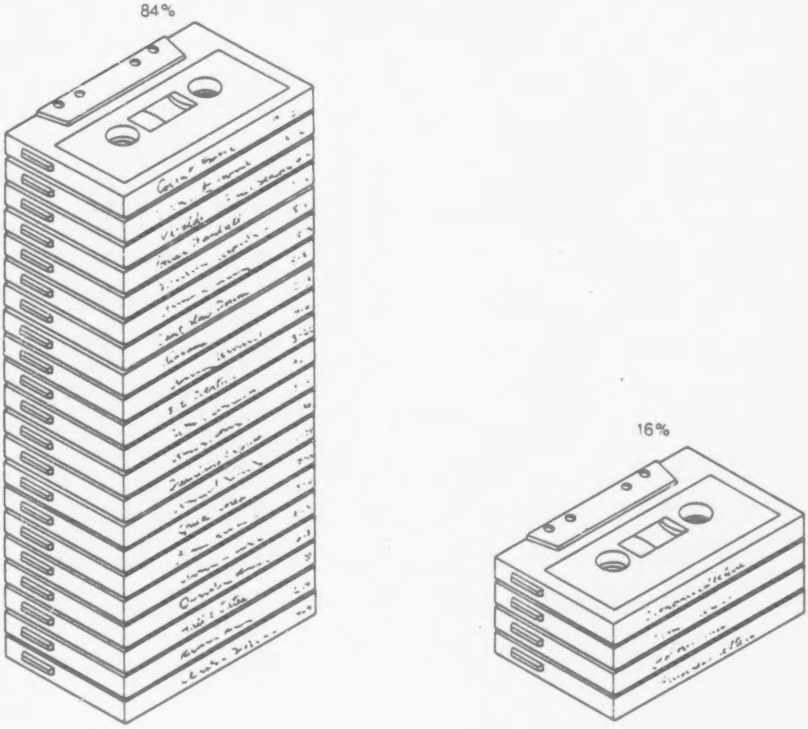
[77] The opponents of the Act attempt to provoke public outcry by labelling the proposed royalty a tax. In fact, it is nothing of the kind. A "tax" is what a government collects for public purposes. A "royalty" is a payment made for the use of a right owned by someone else, in this case the right to record the music that legally belongs to an artist, publisher, or record company.

[78] ARRC Pamphlet at 10. The study prepared for the Electronics Industries Association by Yankelovich, Skelly & White suggests that 52 percent of home taping does not involve copyrighted material. See YSW Report at 14. As was pointed out in an analysis submitted by the National Music Publishers' Association, the Recording Industry Association of America and the Songwriters Guild of America to this Committee in 1983, however, that estimate contains serious methodological flaws. See 1983 Senate Hearings at 233-244.

[79] Audits & Surveys Report at 11.

At least 84% of blank tapes are used to record music.
16% or less are used to record non-copyrighted material.



music in the future. Thus, the 84 percent figure likely understates the percentage of tapes that are used to record music. There should thus be little fear that a significant number of people will pay the music royalty but get no benefit.

Despite these statistical findings, the Act goes to great lengths to insure that tapes or equipment that are not used for infringing purposes will be exempt from royalties.

First, the Act makes clear that no royalty is to be imposed on tapes and equipment used for commercial, professional, educational or similar purposes, such as recording for the blind and disabled. So long as these tapes and equipment are not used for home taping or other infringing purposes, they will not be subject to royalties.

Second, the Act targets the royalty on tapes to those that are suitable for music recording; it specifically exempts from royalties tapes that are -- based on technical criteria -- "unsuitable" for music reproduction. This provision has been added to the current version of the Act in direct response to criticism that opponents of the legislation have voiced for years:

that those who do not use a tape to record copyrighted material should not have to pay a royalty.

Now, in the course of their lobbying efforts, opponents of the Act have argued that one cannot distinguish among tapes based on technical criteria, and that all tape is suitable for recording music.

This is an unsupportable -- and indeed unprecedented -- position. The solution adopted by the Act is premised on the manufacturers' own representations in the marketplace that tapes vary in technical quality -- and hence price. Sony's promotional literature, for instance, identifies "recommended applications" for the cassette tapes it manufactures. As is clear from the excerpt on page 71 -- taken from a Sony Tape Sales Handbook -- Sony believes that its low price standard tape should not be used for taping music, but instead should be used for what the Act would classify as noninfringing uses. Moreover, judging from all the frowning faces at the bottom of the chart, Sony considers its more expensive tapes to be too good for use in connection with business, hobby or study.

Similarly, one of the largest tape retailers in the country describes certain lower priced tapes

SELECTING THE RIGHT AUDIO CASSETTE

To ensure the best possible performance at the lowest possible cost with your equipment and application, Sony recommends the cassette tapes shown below.

SONY TAPE (TYPE)	Recommended Applications			
	Music	Business	Hobby	Study
TYPE I CHF/LNX	☹	☺	☺	☺
TYPE I BHF/HFX	☺	☹	☺	☹
TYPE I AHF/SHF	☺	☹	☺	☹
TYPE II UCX	☺	☹	☹	☹
TYPE II UCX-S	☺	☹	☹	☹
TYPE III Fe-Cr	☺	☹	☹	☹
TYPE IV Metallic	☺	☹	☹	☹

in its most recent catalog as "General Voice Normal Bias" tapes, and will explain to callers that music recorded on such tapes "won't sound very good."

Another leading tape manufacturer, TDK, goes even further and distinguishes among different qualities of music tape: some are claimed to be ideal for "orchestral and operatic" music, while others are promoted for "modern jazz, chamber, progressive rock or discos." Some tapes are recommended for recording from "high-quality LPs," and others for taping "older disks." (*See* the TDK Reference Guide on pages 73-74.) Even more recently, tape manufacturers have begun to promote product lines specifically tailored to recording music from compact discs. (*See* the sample advertisements on pages 14-16.)

If TDK and others can draw such fine distinctions as to recommend the type of music and medium for which each of their high-quality tapes is most suitable, surely they can help the Copyright Royalty Tribunal distinguish between those tapes that are suitable for recording music and those that are not.

The market will also work to minimize any possible problem. As Dr. Greenspan has testified before this

PROFESSIONAL REFERENCE – For The More Discriminating Listener.

The Application. The Right Tape.

Bias: Metal Type IV
EQ: 70μs
60 or 90 min.

SUBJECT: Orchestral and operatic music with exceptional dynamic range recorded from high-quality LPs, digital disks or master tape.

RECORDING EQUIPMENT: High-end component systems with metal position.

PLAYBACK EQUIPMENT: High-end component systems.

SPECIAL FEATURE: Unique metal unibody frame.

TDK
MA-R90
Metal Position

Bias: High (CrO₂) Type II
EQ: 70μs
60 or 90 min.

SUBJECT: Music with consistent loudness in dynamics and [illegible] frequencies such as chamber, progressive rock, jazz or disco recorded live, from quality LPs, digital disks or master tape.

RECORDING EQUIPMENT: Home component systems.

PLAYBACK EQUIPMENT: Home component systems.

SPECIAL FEATURE: First metal formulation for high-bias recording.

Bias: High (CrO₂) Type II
EQ: 70μs
60 or 90 min.

SUBJECT: Music with broad dynamic range such as opera, symphonic, chamber, progressive jazz, soul or rock recorded live, from quality LPs, digital disks or master tape.

RECORDING EQUIPMENT: High-performance component systems.

PLAYBACK EQUIPMENT: Component systems, highest-performance car stereos.

SPECIAL FEATURE: High-density dual-layered Super Avilyn formulation.

TDK
SA-X90
High Position

Bias: Normal Type I
EQ: 120μs
60 or 90 min.

SUBJECT: Music with extended dynamic range such as modern jazz, chamber, progressive rock or disco recorded live from FM or quality LPs.

RECORDING EQUIPMENT: Home component systems, integrated systems.

PLAYBACK EQUIPMENT: Home systems, quality car stereos, headphone portables.

SPECIAL FEATURE: First normal bias Avilyn formulation.

TDK
AD-X90
Normal Position

REFERENCE STANDARD – Recommended For All Premium Applications.

The Application.

The Right Tape.

Bias: Metal Type IV
EQ: 70µs
60 or 90 min.

SUBJECT: Classical music w[illegible] dynamic range recorded from quality LPs or compact digital disks.

RECORDING EQUIPMENT: Top quality component systems with metal positions.

PLAYBACK EQUIPMENT: Fine home component systems with metal positions.

SPECIAL FEATURE: High MOL super-wide dynamic range.

TDK
MA90
Metal Position

Bias: High (CrO$_2$) Type II
EQ: 70µs
60 or 90 min.

SUBJECT: Music with great dynamic range, LP dubbing.

RECORDING EQUIPMENT: Home component systems.

PLAYBACK EQUIPMENT: Home systems, headphone-equipped portables, car stereos.

SPECIAL FEATURE: Most popular high-bias audio cassette in the United States.

TDK
SA90
High Position
HIGH RESOLUTION

Bias: Normal Type I
EQ: 120µs
60 or 90 min.

SUBJECT: Music such as easy listening, pop, contemporary or new wave; older disks.

RECORDING EQUIPMENT: Mid-range and economy component systems, home compacts and combination systems.

PLAYBACK EQUIPMENT: Mid-range component and car systems, portables, and home compacts.

SPECIAL FEATURE: Special formulation for a wider dynamic range and superior MOL.

TDK
AD
Normal Position
EXTENDED HIGH END LOW NOISE HIGH OUTPUT

Bias: Normal Type I
EQ: 120µs
60, 90, 120,*
180* min.

*Not recommended for general applications.

SUBJECT: Music recorded from radio or records; voice recorded from speeches, lectures, interviews or conversation.

RECORDING EQUIPMENT: Home tape deck systems or battery-powered portable recorders.

PLAYBACK EQUIPMENT: Portables, car systems, home and office tape deck systems.

SPECIAL FEATURE: The all-purpose cassette with the widest assortment of lengths.

TDK
D
Normal Position

All specifications subject to change without notice. All audio cassettes have full lifetime warranty. See details on back.

Committee,[80] tape and equipment manufacturers may respond to the Act by designing new products for nonmusic taping needs that would be exempt from royalties. Blank tape manufacturers already market specially denominated "Dictation Tape" and "Computer Cassettes," for example. Consumers are thus likely to be given a range of choices for their nonmusic taping needs, and to have available for business, hobby and study purposes tapes that are not subject to a royalty.

By distinguishing among various types of tapes, the Home Audio Recording Act thus largely eliminates the unfairness of imposing royalties on tapes not used to record music. Such a system might not achieve a perfect fit: there might remain a tiny fraction of total tapes that bear a royalty but that are never used to record music, just as there are likely to be non-royalty bearing tapes that are used to record music. But rejecting the overall legislation because of that possibility would perpetuate a far greater inequity: the denial of any compensation at all to those injured by home taping.

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[80] 1983 Senate Hearings at 103.

C. "The Proposed Royalty Will Unfairly Penalize Those Who Tape Their Own Records"

Opponents of the Home Audio Recording Act also contest imposition of a royalty on the ground that many consumers tape their own records to make customized anthologies or second copies for use in their cars or portable stereos. Opponents contend that those tapers are not displacing record sales and thus assume that they are not hurting anyone by their copying. This contention does not withstand analysis, however.

First, survey evidence rebuts the notion that most tapers are merely taping their own records. As the WCI Survey found, 55 percent of the albums that are taped come from records and prerecorded tapes that tapers do not own, i.e., from borrowed records or tapes or off the air. WCI also found that 61 percent of taped selections come from borrowed records or tapes or from the radio or television.[81] Thus, there is scant basis for the assertion that taping largely involves a taper's own records.[82]

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[81] WCI Survey at 22, 23.

[82] In addition, there is little reason to believe that tapers are taping just to customize anthologies, since the YSW study found that 75 percent of music tapers have taped a complete album -- and, indeed, that 42 percent copied a complete album when they made their last tape from their own music collections. See YSW Report at 66-67.

Second, there is a basic flaw in the argument that taping to make second copies or to customize anthologies does not hurt anyone. While not every act of home taping displaces a sale of prerecorded music, the Audits & Surveys study conclusively demonstrates that taping -- whether done to save money, to make second copies, to customize anthologies or for some other reason -- displaces sales of 325 million albums annually. Consumers are essentially getting those albums for free -- or for the minimal cost of the blank tape used to record them. Consumers do not get second phones for their cars -- or paperback copies of hardcover novels -- without paying for them; nor do they expect to. Why, then, should music be singled out as the only product that consumers can get second, third and fourth copies of without charge? Is there any doubt that the manufacturers of blank tape and equipment would be singing a rather different tune if the new technology enabled customers to make multiple copies of *their* products? The notion that making second copies of one's own albums or prerecorded tapes does not hurt anyone simply does not square with reality: *all* lost sales harm the music community.[83]

The second copy argument also misperceives fundamental principles of copyright law. Our copyright system entitles the copyright owner to compensation for each reproduction or use of his or her creative work. When, as is intended by the copyright laws, everyone pays something for each copy or use, consumers are freed from high prices for any single purchase, performance, or exhibition. When this principle is perverted, however, the consumers who do pay end up paying more -- to subsidize the free riders who pay nothing. The ultimate harm to consumers, the music community, and music in general has been amply described above; it is simply fallacious to claim that those who make "second copies" -- whether of single tunes or of whole albums -- are not causing any injury.

D. "The Proposed Royalty Will Hurt the Music Community's Best Customers"

Another contention advanced by opponents of the legislation is that the proposed royalty will hurt the music community's best customers: home tapers. As explained above, however, the legislation does not "hurt" home tapers; it in fact helps to insure that the music community will continue to be able to produce the music that record buyers and tapers alike want to hear. Tapers are fair-minded enough to perceive that it is in their long-term best interests to protect the rights and careers of those who produce music; without such protection, the very thing they are anxious to tape -- music -- will be in danger of drying up altogether.

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[83] In any event, as discussed in greater detail supra, the royalty rates set by the Home Audio Recording Act will compensate the music community for only a portion of its demonstrated losses. (See pages 53-54.)

Even those who are profiting at the expense of the people who actually create and produce American music -- the predominantly Japanese manufacturers and importers of audio blank tapes and audio recording equipment -- will ultimately benefit from enactment of this legislation. The Act will help to ensure the continued vitality of the American music industry on which they depend for their own success.

E. "Home Taping Stimulates Purchases of Prerecorded Music"

A corollary to the argument that the proposed royalty will only hurt the music industry's best customers is the opponents' claim that home taping stimulates purchases of prerecorded music. It is probably true that home taping stimulates some sales. The problem is that for every sale induced by home taping, the music community loses at least ten others.

As the Audits & Surveys report demonstrates, only a handful of tapers indicate that home taping has anything to do with their decisions to purchase albums. Indeed, only 4.3 percent of respondents listed as a factor in their last purchase decision that they had "heard other music by [the same] artist/group on a home-recorded tape"; even fewer (2.7 percent) mentioned that they had "heard a home-recorded tape of [the recording purchased]." (See page 81.)[84]

If the Audits & Surveys findings are compared to the total sales of albums for 1983 -- the year in which the survey was conducted -- it appears that between 21 and 33 million of the 478 million albums purchased in that year were purchases stimulated by home taping. Twenty-one and 33 million are, however, approximately 6 percent and 10 percent, respectively, of the 325 million sales that Audits & Surveys found are lost to home taping

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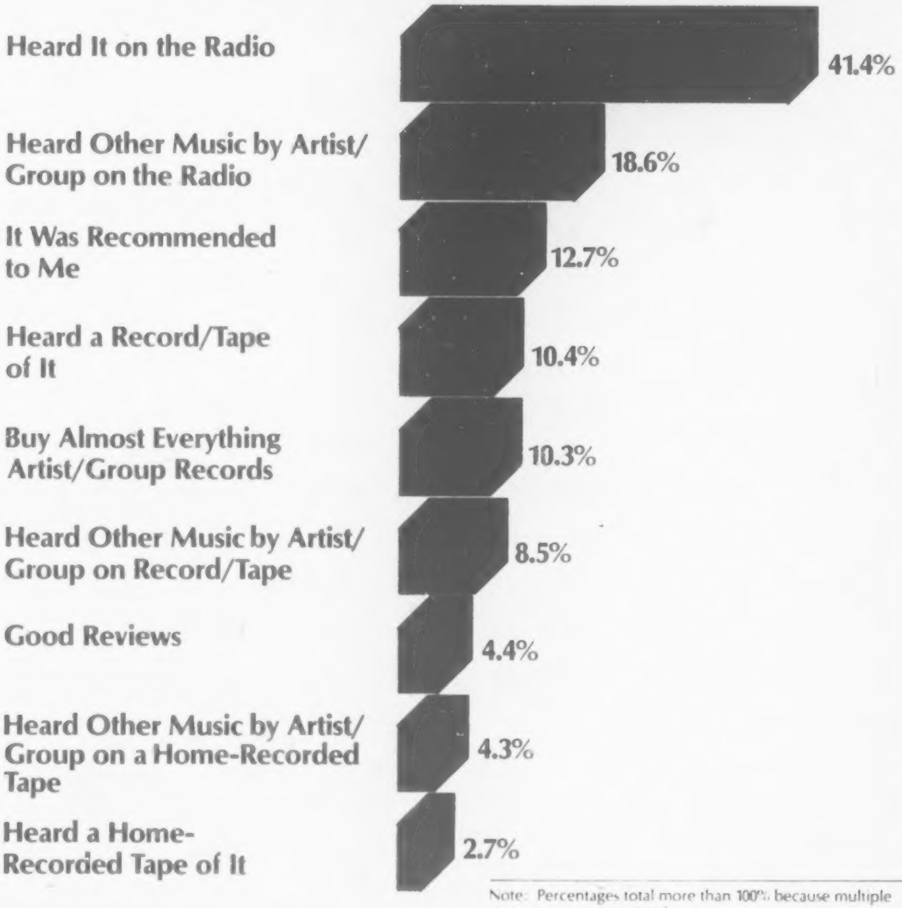
[84] Audits & Surveys Report at 15. The fact that these respondents said that home taping was "a" factor in their purchase decisions does not, moreover, demonstrate that they would have made those purchase decisions had other factors, such as exposure to the music on the radio or knowledge of the artist, not been present as well. Thus, the Audits & Surveys findings likely overstate the stimulus that home taping, taken alone, provides for record purchases.

Reasons for Purchase of Record/Tape



Note: Percentages total more than 100% because multiple responses were permitted.

Source: Interviews of those who taped and purchased one or more recordings in past month every year. The inescapable conclusion, therefore, is that for every record sale the music community gains from home taping, it loses at least ten others.

F. "The Proposed Royalty Will Create an Unwieldy New Bureaucracy"

Contrary to the claim that the proposed royalty will create an unwieldy new bureaucracy, the Act builds upon and extends existing and successful copyright administration systems at little or no cost to the taxpayer. Specifically, the Copyright Royalty Tribunal is an existing government agency, and its administrative expenses for distribution of the proceeds from the compulsory license will be deducted from the royalties paid. Moreover, the Tribunal has developed considerable expertise in the conduct of formal royalty distribution proceedings in connection with its administrative responsibilities for the royalties paid for jukebox and cable television performances.

In addition, as noted above, see pp. 60-61, supra, there are existing systems and data bases that can guide distribution of royalties, both in the United States and abroad. ASCAP and BMI, for instance, maintain data bases which help to distribute performance royalties, and The Harry Fox Agency and the record companies have data on the sales of records and prerecorded tapes. It is simply fallacious to claim, therefore, that the Home Audio Recording Act requires an administrative system that is either innovative or unwieldy.

G. "The Proposed Royalty Will Benefit Only Superstars"

Another specious claim frequently heard is that the proposed royalty will only make rich superstars even richer.

There is no denying that successful artists will benefit from this legislation. But that is how it should be. As owners or beneficiaries of copyrighted property, they are entitled to be paid for its use -- just as Sony is entitled to be paid a royalty when one of its patented compact discs is sold, no matter how well-off that company may already be. This is consistent with property rights generally as well as with basic intellectual property principles.

The reason that the ARRC makes this argument should be obvious -- to divert attention from the huge numbers of artists, songwriters, vocalists and musicians who comprise the vast bulk of the music community.

No doubt, their royalties will be smaller than those earned by the more successful artists, but even a small check to an artist striving to make a career in music can be the difference between success and failure.

Of course, for those who have not even had recordings made of their work, there can be no royalty check, since obviously there cannot have been any displaced sales. But even these unrecorded struggling artists will benefit from this legislation -- for it will generate sorely needed revenues to underwrite new performers, new songwriters, new musicians and new music. The music industry has traditionally relied upon the revenues generated by its few hits to support the investment required for tomorrow's generation of creators. As Beverly Sills once testified before this Subcommittee, it was the success of the Beatles that enabled her record company to finance her operatic recordings.[85]

Thus, for the less established, less popular, or less successful artists, the infusion of revenues from home taping royalties means renewed opportunities and brightened prospects for a career in music. It is not at all surprising, therefore, that the aspiring songwriters, performing artists and musicians of America are so solidly in favor of this legislation, and that their representatives at the songwriter guilds, musicians' and performers' unions, and all the other member organizations of the Coalition to SAVE AMERICA'S MUSIC are working so hard to get this legislation enacted.

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[85] 1981 & 1982 Senate Hearings at 441.

It is not just the superstars, but music as a whole -- the people who create it, and the consumers who enjoy it -- that will benefit from the Home Audio Recording Act.

CONCLUSION

As has been amply demonstrated above, "beating the system" by taping music -- instead of purchasing it -- is both fundamentally unfair and severely detrimental to the future of American music. It is unfair because, quite simply, it duplicates the product produced by hundreds of thousands of working Americans without paying for it. It is detrimental because, equally simply, it endangers the continued ability of the American music community -- and all the artists, producers, composers, music publishers, vocalists, musicians, technicians, and record company personnel who comprise it -- to create the kind of music that has become the most important music in the world.

Numerous countries have recognized the need to protect their own creative work product by enacting legislation that guarantees to music creators a fair and reasonable return for their creative endeavors. This Congress has itself recognized the need to act to insure that the workings of our copyright system keep pace with our technological ingenuity.

The United States cannot now afford to ignore these precedents or the needs of its own creative music community. It cannot afford to lose the jobs and economic support that the music industry provides for hundreds of thousands of working people across the country. Nor can it afford to squander the creative energies nurtured and supported by our music community. Without this legislation, we will all be faced with a world in which the music community cannot spare the resources needed to cultivate and develop new talent and experimental types of music, in which the price of albums and prerecorded tapes will steadily increase to compensate for the loss in sales resulting from home taping, and in which all of us -- artists and consumers -- will be the poorer.

The National Music Publishers' Association, the Recording Industry Association of America, and the Songwriters Guild of America, urge you to enact this legislation as a means of insuring the continued production of the new and diverse music that has always been a hallmark of the American cultural tradition.

Coalition to SAVE AMERICA'S MUSIC!

The Coalition to SAVE AMERICA'S MUSIC represents 25 national music groups, nearly 2.5 million individual members and hundreds of companies.

The objective of SAVE AMERICA'S MUSIC Coalition is to support the passage of The Home Audio Recording Act (S. 1739 in the Senate and H.R. 2911 in the House). We urge Congress to enact it promptly.

Academy of Country Music - Promotes and enhances the popularity of country music.

American Federation of Musicians - Affiliated with the AFL-CIO. Protects the employment rights of professional musicians in all fields in the U.S. and Canada, including collective bargaining agreements.

American Federation of Television and Radio Artists - Negotiates and administers collective bargaining agreements for professional performers and broadcasters for live and taped broadcast performances, phonograph recordings, and audio-visual productions.

Association of Independent Music Publishers - Furthers the interests and education of the independent music publisher in all fields of the publishing industry.

American Music Center - Promotes the creation, performance, publication and recording of American classical music.

American Society of Composers, Authors & Publishers - Founded to license and collect fees for the rights to public performances of its members' copyrighted musical works, and to distribute such income.

American Society of University Composers - National service organization for composers to promote and disseminate the music of its members through their score publications, sound recordings, radio broadcasts and the presentation of public concerts.

Black Music Association - Dedicated to promoting, perpetuating, and preserving black music.

Broadcast Music Inc. - Represents writers and publishers. Licenses, collects and distributes fees for their publicly performed musical repertory.

Country Music Association - Promotes and develops country music worldwide. Activities include annual network television Awards Show, international country music Fan Fair, seminars, research and publications.

Church Music Publishers Association - Preserves and promotes gospel music.

Gospel Music Association - Represents, promotes and spreads the word about gospel music, including presentation of the annual DOVE Awards.

Music Publishers' Association of the United States - Formed to promote the continuing education of music publishers worldwide, and to foster good relationships with the music trade.

Meet The Composer, Inc. - Fosters and promotes the music of living American composers, encourages the commissioning and recording of new music, and develops audiences for the music of our time.

National Academy of Popular Music - Maintains Songwriters Hall of Fame, museum and reference archives on popular music, and annually elects members to Hall of Fame.

National Academy of Songwriters - Protects and educates its nationwide songwriter membership via workshops, forums, inexpensive legal services and a business inquiry hotline.

National Federation of Music Clubs - Finds and fosters young musical talent through Festivals, Young Artist Auditions, Composition contests, awards, scholarships, sponsorship of National Music Week, and representation to the United Nations.

Nashville Music Association - Represents all forms of music entertainment in Nashville.

National Music Council - Umbrella organization chartered by Congress to function as an information and coordination service for 1,5000,000 members.

National Music Publishers' Association - Represents publishers of American music, including fields of popular, classical, sacred, educational, concert, gospel and country music. Collects and administers royalties through the Harry Fox Agency.

Nashville Songwriters Association International - Dedicated to the advancement of musical composition and the protection of member rights. Holds educational seminars.

Recording Industry Association of America - Works for the mutual interest and betterment of the industry. Activities include Anti-Piracy Intelligence Unit and certification of RIAA Gold/Platinum Records Award.

SESAC, Inc. - Licenses and collects fees for use of works of its songwriter and publisher members.

The Songwriters Guild of America - Protects its American songwriter membership through their SGA contract in dealings with music publishers.

Society of Professional Audio Recording Studios - Dedicated to excellence through innovation, communication and education of its recording studio, manufacturer, record company and producer memberships.

Senator MATHIAS. Our next panel is Mr. Jack C. Battaglia, general manager of Memtek Products, Campbell, CA; Mr. Len Feldman, L. Feldman Electronics, Great Neck, NY; Charles Ferris, of the law firm of Mintz, Levin, Cohn, Ferris, Glovsky & Popeo, Washington, DC; Ms. Carol Tucker Foreman, of Foreman & Co., Washington, DC; and Mr. J. Scott Graves, manager, Vesco's Vermont Electric, Woodstock, VT.

Gentlemen, we face that inevitable time problem.

Mr. Ferris is well aware of these problems, so we will appoint him the quarterback.

STATEMENT OF A PANEL CONSISTING OF JACK C. BATTAGLIA, GENERAL MANAGER, MEMTEK PRODUCTS, CAMPBELL, CA; LEN FELDMAN, L. FELDMAN ELECTRONICS, GREAT NECK, NY; CHARLES D. FERRIS, ESQ., OF MINTZ, LEVIN, COHN, FERRIS, GLOVSKY & POPEO; CAROL TUCKER FOREMAN, OF FOREMAN & CO, WASHINGTON, DC; AND J. SCOTT GRAVES, MANAGER, VESCO'S VERMONT ELECTRIC, WOODSTOCK, VT

Mr. FERRIS. Thank you, Mr. Chairman.

Mr. Chairman and members of the subcommittee, my name is Charles D. Ferris. I am an attorney in Washington, DC, and am pleased to have the opportunity of testifying before you on behalf of the Audio Recording Rights Coalition [ARRC].

The coalition is comprised of a diverse group of companies that are involved in the manufacture, sale, and distribution of audio cassette recorders and audio tape, and related equipment. They include 3M, G.E., Pfizer, DuPont, Memtek Products, Maxell, J.C. Penney, Sears, Roebuck & Co., Sony Corp. of America, and Matsushita Electric Corp. of America. Our membership includes many prominent trade associations, such as the Electronic Industries Association, the American Retail Federation, the National Retail Merchants Association, along with various consumer groups, thousands of individual retailers, and educational organizations.

We appreciate the opportunity to testify on home audio taping and to explain to the subcommittee how millions of Americans have enjoyed what have always been completely legal activities; indeed, Congress itself, in the Sound Recording Act of 1971, ratified existing law and explicitly reaffirmed the legitimacy of home taping. Specifically, I would like to focus on why a royalty tax is entirely unwarranted—the recording industry is making more money now than ever before—and anticonsumer-enriching record companies at the multimillion-dollar expense of the American public. Coupled with the fatal overbreadth of S. 1739 and other similar legislative proposals, the industry's extraordinary wealth demonstrates all too clearly that there is no need for taxes on audio recording equipment and tape.

As we have stated consistently to this subcommittee over the past few years, the coalition unequivocally supports protecting and preserving the right of the public to engage in private, noncommercial recording of audio materials. It opposes any legislation, including S. 1739, that would tax individuals for private taping activities.

SOME FUNDAMENTAL PRINCIPLES AND AN OVERVIEW

I would like to begin with two fundamental principles that are the bedrock of the ARRC's opposition to royalty taxes on audio recorders and blank tapes.

First, the recording industry is dead wrong in its simplistic view that home taping results in enormous lost sales. Substantial amounts—up to one-half—of home taping involve no use of copyrighted material. Most home music taping is from tapers' own collections and is to make purchased music portable and more convenient, or to preserve it. Indeed, much home taping stimulates sales of prerecorded music. These facts are substantiated by several studies that I will discuss later in my testimony.

Moreover, home taping is not a ready substitute for prerecorded music. Many home-recorded tapes are not available on the market. They consist of selections put together by consumers from various sources. Or, they are tapes of music that has not been released, or is difficult to find, in cassette format. Home tapes, in addition, may be the only way for consumers who want music in a cassette format of high quality to avoid the inferior tapes produced by record companies. Much home taping, therefore, is a direct result of the recording industry's own failures to offer the public what it wants.

The industry's many purported analyses of injury from home taping conspicuously omit the benefits that it realizes from the widespread marketplace penetration of recording technology. In addition to the stimulative effect of taping behavior on the purchase of prerecorded music, home recording technologies have created vast marketplace opportunities for record companies and for the broader creative community. The boombox, the car stereo, and walkman-type players have made it possible for the industry to more than double its sales of prerecorded cassettes from 1981 to 1984. Thus, before deciding to impose economic constraints on home taping and home taping technologies, it is critical that their net impact on creative artists be understood.

Before leaping to the conclusion that there is, in fact, a home taping problem that would justify any remedy, let alone a remedy as fundamentally flawed as S. 1739, a complete analysis of the economic relationships that bind creators and technology is needed.

The second fundamental principle is that all the proposals to find a remedy to what is a nonexistent problem are inherently overbroad because they would tax a wide range of uses of recorders and tape that have no conceivable impact on the recording industry. The purported solution of S. 1739 to this flaw is unworkable in that it is essentially impossible to classify tape or recorders as suitable for taping music.

Furthermore, the overbreadth endemic in S. 1739 or any other such tax proposal will be exacerbated greatly in the future. We are in the middle of a revolution in which there is widespread use of high fidelity video recorders for recording sounds, where audio and video technologies are merging in a new 8-millimeter format, and where audio, video, and data storage technologies are fusing. To impose an economic burden on a single technology of today would inevitably distort the course of tomorrow's technological development by encouraging untaxed over taxed technologies.

The bureaucratic mechanics of S. 1739 ensure that any stimulus to creativity that might be generated by the royalty funds will be dissipated. The procedure guarantees litigiousness by copyright owner claimants and delays in distribution. Of even greater concern is that responsibility for periodic adjustment of the amount of the levy and for disbursal of the proceeds is vested in the overburdened Copyright Royalty Tribunal.

The poverty of the recording industry's case against home taping stands in stark contrast to the riches of its own larder. Some years back, the industry tried to rest its case for special relief on a slump in sales alleged to be caused by home taping. Now, however, the industry must confront an embarrassment of riches as industry sales and profits have reached all-time highs.

Over 3 years ago, before this subcommittee, we stressed that the problems facing the recording industry did not stem from home taping, but were of its own making. Recent experiences—and the industry's own efforts to face up to excessive costs—are the best rebuttal of its past and present claims as to the harm allegedly resulting from home taping.

Then, as now, a royalty tax on consumers is tantamount to an annual windfall of hundreds of millions of dollars for the recording industry. Given the extraordinary prosperity of the industry, there can be no doubt whatsoever as to the sufficiency of market-generated incentives for copyright owners.

In yet again addressing home taping issues in response to the industry's latest pleas for relief, neither we nor the Congress do so on a blank slate. Last year, in its decision in *Sony* v. *Universal City Studios,* the Supreme Court struck the proper balance of the copyright law, weighing the interests of copyright owners with the rights of the American public to recognize the legality of home video taping. Nearly 15 years ago, in the 1971 Sound Recording Act, Congress itself acknowledged the legitimacy of noncommercial home audio taping. Those who now urge that the earlier and time-tested wisdom of Congress and the Court should be altered—and a royalty tax imposed on those who tape—have the burden of demonstrating why such change is needed.

We believe that the proponents of royalty taxes once again have failed to make their case. Congress should reject, once and for all, any tax schemes on audio recorders and tape.

HOME AUDIO TAPING BENEFITS COPYRIGHT OWNERS

The cardinal tenet of the recording industry case—that home audio taping hurts sales—is wrong. In analyzing the industry's arguments and the wisdom of taxing home tapers, it is important to recognize that there are many different kinds of home taping. Many of these stimulate, rather than displace, sales of prerecorded music. The recording industry would like Congress to believe that the story is simple. To focus, however, only on alleged harm caused by home taping, and to ignore the extent to which it benefits copyright owners, is to tell only half the tale.

Surveys consistently show that taping leads to decisions to purchase prerecorded music. A survey prepared by Yankelovich, Skelly and White, Inc., for the Audio Recording Rights Coalition, entitled "Why Americans Tape: A Survey of Home Audio Taping In the United States" ("Yankelovich Survey"), found that over half of all home tapers often or sometimes buy a record after having made a tape of the same record or of selected songs from it.

That home taping and the purchasing of prerecorded music are involved in a synergistic, not predatory, relationship is further demonstrated by the fact that over half of all home music tapes are made from music in a taper's own collection—music that has been bought and for which royalties have already been paid. It is equally critical to recognize that tapers also regard the ability to tape music—whether to preserve it or to make it portable so that it can be enjoyed in a personal or car stereo—as a key element of the value of the music. Thus, that music can be and is being taped is not to be bemoaned as being detrimental to the industry; instead, it is an essential part of the motivation for purchasing music in the first place.

The relationship between purchasing and taping music is, therefore, synergistic. Tapers are more interested in prerecorded music than nontapers, and, not surprisingly, they spend much more money on music than those who do not tape. Each activity reinforces the other. The words of Rolling Stone magazine of some 3 years back are as true today as they were then: by taxing tapers, the recording industry is branding "its best customers"—the "very people" on whom it "depends . . . to turn a release platinum"—as "its worst enemies."

THE RECORDING INDUSTRY FAILS TO RECOGNIZE THAT HOME TAPING TECHNOLOGY IS NOT AN ENEMY—BUT IS ONE OF ITS GREATEST FRIENDS

The industry has reaped enormous economic rewards from recording technologies. The widespread availability of home taping technology has opened multibillion dollar markets for the recording industry and unparalleled opportunities for the creative community.

The public has embraced recording technology. Sales of prerecorded cassettes now have far surpassed those of LP's, with music in the cassette format outselling disks 2 to 1. The billions of dollars in sales of prerecorded cassettes, or of records that are, in part, bought to be taped, are ample bottom line testament that technology is an ally of artists and record companies.

It is the massive endorsement of recording equipment by tens of millions of American consumers that has laid the foundation for the skyrocketing penetration of playback devices for which ever-increasing amounts of music are being purchased. As Russ Solomon, president of Tower Records, said in an interview last year:

> [I]f you did not have the home-recording business, you would not have Walkman machines. In other words, the tape technology that came out of the recording machine resulted in the portable playback machine and the automobile machine, which created an enormous market for us.

To shun technological change—to view it as an enemy that should be subjugated economically to the interests of copyright owners—defies economic reality and common sense. Copyright owners historically have been all too dismissive of the benefits that they realize from the creative efforts of other products that create or expand markets for sound recordings or audiovisual works.

MUCH HOME TAPING IS CAUSED BY RECORD COMPANY RELUCTANCE TO ADAPT TO TECHNOLOGICAL CHANGES AND CONSUMER PREFERENCES

The recording industry is no exception to the general principle that copyright owners are slow to recognize the benefits that technology can bring. Beginning in the late 1970's, consumers wanted portability, convenience, and high quality in their music. They realized the advantages of cassette technology in giving them what they wanted and so the public began purchasing car stereos, portable stereos, and walkman-type players. The record companies, however, long after consumer preferences had changed, were still turning out LP's and other black vinyl product. It came, then, as no surprise to anyone but the record companies, that industry sales and profits slumped in the early 1980's: record companies simply were not making what consumers demanded.

Even today, the recording industry has yet to embrace fully the many opportunities created by the technological revolution. Prerecorded cassettes are still, for some music, harder for consumers to obtain than records. They are not, in many cases, released simultaneously with LP's. Record companies persist in using poor-quality tapes, recorded at high speeds, and with shorter playing times for the distribution of prerecorded music on cassettes.

Tapers have, therefore, been forced to turn to home taping to obtain the qualities that they cannot otherwise get in the marketplace. Home-recorded tapes can have longer playing times or may be made of tape of better quality than that used by the record companies for prerecorded cassettes. Tapers archive their records, to preserve the music that they own and to listen to it without the wear and tear inherent in repeated phonorecord playback. Tapers want to take high-quality sound with them when they jog, lie on the beach, or drive to work.

Contrary to the cries of copyright owners, then, home taping technology is extraordinarily beneficial to the recording industry. No compensation in the form of royalty taxes should be extracted either from those who developed that technology or from home tapers.

Such pleas for compensation are even less seemly when it is evident that the industry's very own lethargy or myopia with respect to technology has been a major impetus for home taping behavior. Viewed in this broader context, to propose that a royalty tax ought to be paid to record companies is wholly unjustified.

THE RECORDING INDUSTRY'S ECONOMIC RECOVERY UNDERCUTS ITS CLAIM FOR COMPENSATION FROM HOME TAPING ACTIVITY

The hollowness of the recording industry's clamor for legislative relief is underscored by its record profits and sales in 1983, 1984, and, now, 1985. Although record companies have been arguing for over 4 years that a royalty tax is justified because sales of prerecorded music should have been higher in the late 1970's and early 1980's, the current boom demonstrates what everyone else has long realized: home taping is nothing but a convenient scapegoat.

THESE ARE THE INDUSTRY'S BEST YEARS EVER

Last year the recording industry had its best year ever, with revenues rising 15 percent to $4.37 billion, exceeding the previous record set in 1978, of $4.13 billion. In 1984, virtually every company had a banner year of profits and revenues. The performance of the industry in 1985 is outpacing the record rates of 1984, with gains at retail in the first half of the year of as much as 20 percent over 1984. The industry has totally recovered from its downturn of some years back. No legislative relief is necessary for an industry that is, by all accounts, doing just fine.

THE INDUSTRY'S PAST PROBLEMS HAD LITTLE TO DO WITH HOME TAPING

That home taping was merely a scapegoat was noted at the time by some record company executives and industry observers. Today, the facts demonstrate that these critics within the recording industry—as contrasted with the industry's lobbyists—were right. Some of the causes for the slump—and for the recovery—admittedly were beyond the immediate control of the industry. As the economy improved, it carried sales of prerecorded music along with it. The videogame fad, which had siphoned billions in disposable income, ended.

Other factors contributing to the downturn were very much the result of industry marketing failures. The industry had been slow to adjust to the demand for portability and convenience. As it began to do so, however, markets created by new products, such as the Walkman and the boombox, boosted record company sales of prerecorded cassettes. In 1984, cassettes overtook albums as the preferred format, with the dollar value of cassette shipments representing over 55 percent of the industry's total revenues.

The industry also began applying some sound principles of financial management to its operations. It began cutting costs, ending some of the extravagant practices of the late 1970's. The industry increased cash flow, by adopting new payment and returns policies; these policies have, however, while bolstering industry bottom lines, also had the effect of hampering retailer flexibility to market aggressively. The industry also reduced staff and tightened artist rosters by moving cautiously on signing new artists and letting go older, marginal acts.

These efforts at financial consolidation bear further discussion because the music industry is blaming home taping for the recent decrease in new releases. In light of the record high revenues in 1984, the decision to reduce the number of new releases cannot be based on low industry coffers but rather, I suspect, reflects an internal business judgment by industry executives that it is more profitable for them to place greater emphasis on fewer acts. It is inconceivable that the record companies would revert to their less efficient and less profitable approach, even if they received more money from consumers. Taping is not the real reason for fewer releases and the tax will not necessarily increase releases at all.

At the same time as the industry began adopting these new efficiency measures, it also began to sell the stars it retained. It is hard, indeed, to blame home taping for imagined record company ills when last year saw the release of multimillion seller mega-albums by Michael Jackson, Bruce Springsteen, Prince, Lionel Richie, and Chicago. Such phenomenal success belies the industry's argument that home taping practices have made it difficult to make a profit at the top end of the market. Michael Jackson's Thriller album is the biggest seller of all time—and how necessary is a royalty tax to stimulate creativity when he made $70 million from the sales of that album?

The industry also began promoting its music in ways that aroused public interest. The use of music video has been the major engine of the industry successes of the eighties. Whether on music video television programs, through video clip tours, or by cross-promoting with prerecorded videocassettes, the record companies are finally starting to use some of the technologies that are changing, and benefiting, the industry. At the same time, radio airplay, the traditional promotional tool, has been reinvigorated by video promotion.

Three years ago Congress was right to recognize the unfairness of enacting a legislative cure for ailments that were largely of the industry's own making. Confronted with problems and having had its pleas for a bailout rejected by Congress, the industry was forced to develop and apply its own corrective measures. And those steps have made a difference, contributing significantly to the phenomenal success of the last couple of years. Now, faced with pleas from an industry that has never been healthier, there is even less reason than before for Congress to saddle millions of American consumers with the costs of a Federal handout.

ROYALTY TAXES ARE UNWARRANTED AND WOULD PROVIDE AN UNJUSTIFIED WINDFALL FOR THE RECORDING INDUSTRY

Most home taping activities are not of the type complained of by the recording industry, and others actually stimulate sales of prerecorded music. Against the backdrop of the economic realities of the recording industry, and with an understanding of how home taping has been used as a scapegoat by proponents of a royalty tax, it is important to return to a fundamental proposition. That is, a home-recorded tape does not equal the lost sale of a prerecorded album or cassette. Rather, home taping describes a set of different and interrelated activities, each of which has its own economic consequences.

First, a great deal of home taping, over half, according to the results of the Yankelovich Survey, does not involve prerecorded music. People tape their own performances of music, dictation, telephone messages, family occasions, language or music lessons, rehearsals, lectures, letters to relatives, bird calls, computer programs, along with literally hundreds of other sounds. No compensation is owed to record companies, nor should any be imposed, for all these kinds of taping.

Moreover, the recording industry argument that home-recorded tapes displace sales of prerecorded music is difficult to square with actual home taping activity. Home-recorded tapes that do not contain music are not simple substitutes for prerecorded music. By far, the most common home music taping activity is putting together musical selections for a customized home-recorded tape. Such tapes are, by definition, unavailable on the marketplace: when they are made, there is no displacement. At the same time, the demand for particular songs desired for a selection tape can stimulate—not impair—sales of prerecorded music.

ROYALTY TAXES WOULD CONSTITUTE DOUBLE PAYMENT TO COPYRIGHT OWNERS

A royalty tax would force home tapers to pay a second time for their use of prerecorded music. When consumers buy prerecorded music, they are not just purchasing a piece of vinyl or some magnetic tape in a shell. They purchase the right to enjoy the music. When they tape that music for their car, their portable stereo, or at the office, they are simply extending the area in which they can enjoy what they have bought.

As noted previously, the surveys are unanimous in agreeing that most home music taping is from tapers' own collections. Such taping is simply an enhancement of prerecorded music for which the purchase price, including a royalty, has already been paid to the copyright owner.

Taxing the predominant home music taping activity—taping by individuals of music in their own collections—implies that music lovers should be forced to buy multiple copies of the same music or be economically constrained from making customized compilations of material in their own collections. Thus, unless the recording industry is contending that music can only be enjoyed by consumers in one location and at one time, or that consumers should be penalized for home taping, a royalty tax constitutes unwarranted double compensation for copyright owners.

Even as to the borrowing and taping of prerecorded material, it is far from clear that that activity should be taxed. Sharing belongings with friends or within a family is an ordinary part of human conduct. With respect to copyrighted material, such as books and records, copyright law recognizes the importance of exchanging and disseminating works. Indeed, the law contemplates that the ability to share prerecorded music is an element of the price that is paid to copyright owners. With respect to music, it is only natural that friends or relatives want to share what they own and enjoy. Taping may also occur because record owners want to ensure proper handling of records in their collections.

In deciding whether additional compensation should be coerced from individuals who engage in such normal social interaction, it is important to note that lending and borrowing does stimulate interest in the album or music of the artist that was exchanged. In some instances, moreover, friends may pool resources to buy, and share, an album or cassette that, on their own, none could afford to buy. In short, royalty tax payments to record companies should be rejected because it is clear that, for most home taping activity, one, there has been a purchase of prerecorded music, and, two, there has been or will be no displacement of sales of prerecorded music.

S. 1739 IS OVERLY BROAD, ARBITRARY, AND UNWORKABLE; IT WILL DISTORT TECHNOLOGY AND ALTER THE EXISTING BALANCE BETWEEN THE TECHNOLOGICAL AND ARTISTIC COMMUNITIES

The proposal to tax audio recorders and tape, S. 1739, has a number of flaws that are irremediable: One, the tax is overbroad and would tax all uses of audio recorders and tape; Two, the level of the tax is arbitrary; Three, taxing recording equipment and media will inevitably distort technological development; Four, the proposal uses a mechanism for distribution that cannot carry out the task in a way that will generate incentives for creators; and Five, in direct contravention of the Supreme Court holding in *Sony Betamax* v. *Universal City Studios*, the legislation grossly expands the concept of contributory infringement.

THE TAX IS UNFAIRLY OVERBROAD

Regardless of whether a purchaser of audio equipment of tape uses them to record copyrighted music, he or she would be forced to pay a royalty tax. Such a tax is particularly unfair for those who never or seldom use their recorders to tape prerecorded music. Recognizing the obvious unfairness of such a tax, the industry proposal uses a surrogate for actual use—types of tape—in an attempt to exempt certain users from paying the record companies. Conferring authority on the Copyright Royalty Tribunal to exempt products that are not suitable for taping copyrighted material is, however, no solution to the overbreadth problems of S. 1739.

First, as Len Feldman will explain in greater detail, it is technically impossible to segregate tape by type. This subcommittee heard testimony, in October 1983, that tapes cannot be categorized by their purported lack of suitability for the taping of music. Nothing has changed since that time. The decision to use a particular kind of tape depends on individual economic resources, the importance ascribed by the taper to high fidelity, the need to preserve data, the hardware available, or a myriad of other factors. The simple truth is that people use all kinds of tape and equipment to tape all kinds of sounds.

Furthermore, the exemption provisions of the recording industry proposal are imprecise and inequitable and, consequently, likely to result in abuse. They would impose taxes on machines that could be used for taping prerecorded music, but seldom or never are. Although S. 1739 purports to require the CRT to exempt classes of users who use recorders and tapes for business, the proposal is flawed. Many users, equally as deserving as those that the bill would purportedly exempt, would not be exempted. There is no way around the fact that the bill—and any taping tax—would discriminate against a large class of individual purchasers of equipment who do not engage in home taping.

Without describing in detail the nightmares presented by administration of the exemption provisions, it is clear that they are shams. Not only will they not work in practice, it is probable that they are not even meant to do so. Indeed, the problems with handling the literally millions of annual claims for exemption, reimbursements, and, possibly, a dual inventory scheme of taxed and untaxed products are so massive that they do nothing toward solving the problems of overbreadth. The exemption provisions, in short, are entirely unworkable; nevertheless, no system is fair without providing for an exemption. The only solution is no tax at all.

THE PROPOSED AMOUNT OF THE TAX IS ARBITRARY

Although the intent of the royalty tax legislation is to compensate copyright owners for any losses from home taping, the amount of the levy—5 percent on audio recorders, 25 percent on dual cassette recorders; 1 penny per minute on blank tape—is simply pulled out of thin air. There have been no comprehensive studies of the overall, net financial impact of home taping on copyright owners. It is not surprising, therefore, that the only relationship between the amount proposed by S. 1739 and either the amount of home taping or the level of any purported damage from taping practices is an arbitrary one.

A ROYALTY TAX WILL DISTORT TECHNOLOGY

Imposing a royalty on some products, but leaving others untaxed, will significantly intrude on technological decisions about the future course of consumer electronics technology that are best made in the marketplace. Manufacturers will have substantial incentives to reconfigure products to avoid the levy. At the least, to satisfy consumer demand, they may be inclined to move the taxable recording components into separate, low-cost units to maintain lower prices.

More dangerously, subsequent developments will be skewed by, or overtake, any classification schemes that focus on technology at a single point in time. It is difficult now and will become impossible in the future to make the neat classifications that the proponents of S. 1739 would prefer. For example, videocassette recorders are used to make high-quality, long-playing sound recordings. Video and audio technologies are fusing in the new 8-millimeter standard. Stereo sound is becoming a standard element of television broadcasts and prerecorded videocassettes.

Yet, the proposal contemplates that the CRT will consider regulations that would impose a tax on suitable technology. Decisions to tax videorecorders under S. 1739, or spending an extended period of time in resolving the issue of whether video and mixed audio/video equipment is covered by the bill, will inhibit innovation in consumer electronics.

More broadly, the ongoing task of analyzing developments, continually classifying new products, and conducting searching examination of the technological marketplace is Government intervention with a vengeance. Manufacturers will be required to submit to the CRT proprietary information about the characteristics of new tape and recording equipment products. It may be difficult to provide adequate safeguards against disclosure of such commercially sensitive information.

One result of the proposed exemption scheme, therefore, may be to force proprietary product information into the public domain, with the serious consequence of impairing the competitive relationships that now characterize the tape and equipment market. In sum, governmental oversight of the process of developing new consumer electronics products, as required by the royalty tax proposals, would be intrusive and likely to stultify competition and new entrepreneurial activity.

THE DISTRIBUTION MECHANISM IS UNWORKABLE AND WILL NOT PROVIDE INCENTIVES FOR CREATORS

The mechanism for distributing funds is fundamentally flawed because the CRT, the agency with the responsibility for disbursing the royalty proceeds to copyright owners, is beset with problems. The CRT is now in danger of being disbanded due to problems that include its inadequate staffing and its approach to the tasks with which it is charged under the copyright law. Two bills have been introduced in this session of Congress to overhaul it. The experience to date with the CRT has shown, repeatedly and consistently, that it simply does not have the continuity, expertise, and coherence to perform the distribution function.

The distribution procedure gives prominent play to claimant negotiations that might culminate in a voluntary agreement regarding the distribution of the royalty fees. The hope that such agreement can be reached is nothing more than wishful thinking. The number of claimants involved, the absence of any agreed methodology for measuring the amount of home taping either in the aggregate or for particular songs, the bill's utter lack of any criteria to guide the distribution process, and the consistently contentious character of all other proceedings before the CRT all leave little room for optimism that the claimants would or could resolve their differences expeditiously.

Nevertheless, if copyright owners do not agree as to what each should receive, they will find themselves litigating before the CRT in a proceeding that is bound to be lengthy and intrusive. Moreover, correlating a home taping event and the receipt of compensation will be extraordinarily difficult.

The inability to correlate any actual home taping with compensation for it, coupled with the delay in distribution, will create substantial uncertainty for record companies with respect to the receipt of royalties. It will be nearly impossible for them to rely on proceeds from the royalty fund in evaluating the profitability of particular artists or kinds of music. The royalty tax proceeds, therefore, will not serve their intended purpose—as an incentive for the creation of copyrighted works demanded by the public.

ENACTMENT OF AN EXPANDED CONCEPT OF CONTRIBUTORY INFRINGEMENT WILL CONFER ON THE RECORDING INDUSTRY UNWARRANTED POWER OVER THE ELECTRONICS INDUSTRY

S. 1739 deceptively grants consumers a home taping exemption while forcing them to pay a new tax for engaging in practices that the bill ostensibly legitimates. Congress should be aware, however, that by codifying the concept of contributory infringement it is enacting legislation that is directly at odds with the Supreme Court approach of the *Sony* decision. More fundamentally, the contributory infringement sections of the bill would accord the recording industry nearly unconstrained new power to seek relief from equipment and tape manufacturers.

At the heart of the recording industry proposal is the notion that manufacturers should be liable for how the public uses their products. With respect to home taping, it circumvents the Supreme Court holding in *Sony* by making manufacturers and importers liable for home taping—a liability not now imposed by the law. By invoking these provisions, copyright owners would have plenary power over product development in the electronics industry, completely tilting the state of market equilibrium between the technological and artistic communities that currently prevails.

The recording industry has been trying for years to cure the defects in its various proposals to tax recording technology and tens of millions of home tapers. It has yet to succeed. The truth is that the industry has done phenomenally well, and home taping has helped it to fabulous successes. The industry's attempts to extract more money from the American public have never been seemly. Today, however, with the industry's own pockets overflowing, there has never been a better time to reject royalty taxes as an idea whose time will never come.

Thank you, Mr. Chairman.

Senator MATHIAS. Thank you, Mr. Ferris.

[Mr. Ferris' submissions for the record follow:]

PREPARED STATEMENT OF CHARLES D. FERRIS

Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P. C.,
for the
Audio Recording Rights Coalition
Before the Senate Judiciary Subcommittee
on Patents, Copyrights and Trademarks
on S. 1739

Mr. Chairman and members of the Subcommittee, my name is Charles D. Ferris. I am an attorney in Washington, D.C., and am pleased to have the opportunity of testifying before you on behalf of the Audio Recording Rights Coalition ("ARRC").

The Coalition is comprised of a diverse group of companies that are involved in the manufacture, sale, and distribution of audio cassette recorders and audio tape, and related equipment. They include 3M, G.E., Pfizer, DuPont, Memtek Products, Maxell, J.C. Penney, Sears, Roebuck & Co., Sony Corporation of America, and Matsushita Electric Corporation of America. Our membership includes many prominent trade associations, such as the Electronic Industries Association, the American Retail Federation, the National Retail Merchants Association, along with various consumer groups, thousands of individual retailers, and educational organizations.

We appreciate the opportunity to testify on home audio taping and to explain to the Subcommittee how millions of Americans have enjoyed what have always been completely legal activities; indeed, Congress itself, in the Sound Recording Act of 1971, ratified existing law and explicitly reaffirmed the legitimacy of home taping. Specifically, I would like to focus on why a royalty tax is entirely unwarranted -- the recording industry is making more money now than ever before -- and anti-consumer -- enriching record companies at the multi-million dollar expense of the American public. Coupled with the fatal overbreadth of S. 1739 and other similar legislative proposals, the industry's extraordinary wealth demonstrates all-too-clearly that there is no need for taxes on audio recording equipment and tape.

As we have stated consistently to this Subcommittee over the past few years, the Coalition unequivocally supports protecting and preserving the right of the public to engage in private, noncommercial recording of audio materials. It opposes any legislation, including S. 1739, that would tax individuals for private taping activities.

I. Introduction: Some Fundamental Principles And An Overview

I would like to begin with two fundamental principles that are the bedrock of the ARRC's opposition to royalty taxes on audio recorders and blank tape.

First, the recording industry is dead wrong in its simplistic view that home taping results in enormous lost sales. Substantial amounts -- up to one-half -- of home taping involve no use of copyrighted material. Most home music taping is from tapers' own collections and is to make purchased music portable and more convenient, or to preserve it. Indeed, much home taping stimulates sales of prerecorded music. These facts are substantiated by several studies that I will discuss later in my testimony.

Moreover, home taping is not a ready substitute for prerecorded music. Many home-recorded tapes are not available on the market. They consist of selections put together by consumers from various sources. Or, they are tapes of music that has not been released, or is difficult to find, in cassette format. Home tapes, in addition, may be the only way for consumers who want music in a cassette format of high quality to avoid the inferior tapes produced by record companies. Much home taping, therefore, is a direct result of the recording industry's own failures to offer the public what it wants.

The industry's many purported analyses of injury from home taping conspicuously omit the benefits that it realizes from the widespread marketplace penetration of recording technology. In addition to the stimulative effect of taping behavior on the purchase of prerecorded music, home recording technologies have created vast marketplace opportunities for record companies, and for the broader creative community. The "boombox," the car stereo, and "walkman"-type players have made it possible for the industry to more than double its sales of prerecorded cassettes from 1981 to 1984. Thus, before deciding to impose economic constraints on home taping and home taping technologies, it is critical that their net impact on creative artists be understood.

Before leaping to the conclusion that there is, in fact, a home taping "problem" that would justify any "remedy," let alone a "remedy" as fundamentally flawed as S. 1739, a complete analysis of the economic relationships that bind creators and technology is needed.

The second fundamental principle is that all the proposals to find a "remedy" to what is a non-existent "problem" are inherently overbroad because they would tax a wide range of uses of recorders and tape that have no conceivable impact on the recording industry. The purported "solution" of S. 1739 to this flaw is unworkable in that it is essentially impossible to classify tape or recorders as "suitable" for taping music.

Furthermore, the overbreadth endemic in S. 1739 or any other such tax proposal will be exacerbated greatly in the future. We are in the middle of a revolution in which there is widespread use of high fidelity video recorders for recording sounds, where audio and video technologies are merging in a new eight millimeter format, and where audio, video, and data storage technologies are fusing. To impose an economic burden on a single technology of today would inevitably distort the course of tomorrow's technological development by encouraging untaxed over taxed technologies.

The bureaucratic mechanics of S. 1739 ensure that any stimulus to creativity that might be generated by the royalty funds will be dissipated. The procedure guarantees litigiousness by copyright owner claimants, and delays in distribution. Of even greater concern is that responsibility for periodic adjustment of the amount of the levy and for disbursal of the proceeds is vested in the overburdened Copyright Royalty Tribunal.

The poverty of the recording industry's case against home taping stands in stark contrast to the riches of its own larder. Some years back, the industry tried to rest its case for special relief on a slump in sales alleged to be caused by home taping. Now, however, the industry must confront an embarrassment of riches as industry sales and profits have reached all-time highs.

Over three years ago, before this Subcommittee, we stressed that the problems facing the recording industry did not stem from home taping, but were of its own making. Recent experiences -- and the industry's own efforts to face up to excessive costs -- are the best rebuttal of its past and present claims as to the harm allegedly resulting from home taping.

Then, as now, a royalty tax on consumers is tantamount to an annual windfall of hundreds of millions of dollars for the recording industry. Given the extraordinary prosperity of the industry, there can be no doubt whatsoever as to the sufficiency of market-generated incentives for copyright owners.

In yet again addressing home taping issues in response to the industry's latest pleas for relief, neither we nor the Congress do so on a blank slate. Last year, in its decision in Sony v. Universal City Studios, the Supreme Court struck the proper balance of the copyright law, weighing the interests of copyright owners with the rights of the American public to recognize the legality of home video taping. Nearly fifteen years ago, in the 1971 Sound Recording Act, Congress itself acknowledged the legitimacy of noncommercial home audio taping. Those who now urge that the earlier and time-tested wisdom of Congress and the Court should be altered -- and a royalty tax imposed on those who tape -- have the burden of demonstrating why such change is needed.

We believe that the proponents of royalty taxes once again have failed to make their case. Congress should reject, once and for all, any tax schemes on audio recorders and tape.

II. Home Audio Taping Benefits Copyright Owners

The cardinal tenet of the recording industry case -- that home audio taping hurts sales -- is wrong. In analyzing the industry's arguments and the wisdom of taxing home tapers, it is important to recognize that there are many different kinds of home taping. Many of these stimulate, rather than displace, sales of prerecorded music. The recording industry would like Congress to believe that the story is simple. To focus, however, only on alleged harm caused by home taping, and to ignore the extent to which it benefits copyright owners, is to tell only half the tale.

Surveys consistently show that taping leads to decisions to purchase prerecorded music. A survey prepared by Yankelovich, Skelly and White, Inc. for the Audio Recording Rights Coalition, entitled "Why Americans Tape: A Survey of Home Audio Taping In the United States," ("Yankelovich Survey") found that over half of all home tapers often or sometimes buy a record after having made a tape of the same record or of selected songs from it.[1]

That home taping and the purchasing of

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[1] Yankelovich Survey at 16, 45-48. The flaws in the recording industry case and surveys stem from its failure to understand that the nexus between taping and purchasing is far more complex than that of simple cause and effect. Home taping often fuels the desire to purchase more of an artist's work to complete a collection, or it may introduce the taper to new musical selections or artists, thereby stimulating sales of prerecorded music.

prerecorded music are involved in a synergistic, not predatory, relationship is further demonstrated by the fact that over half of all home music tapes are made from music in a taper's own collection -- music that has been bought and for which royalties have already been paid.[2] It is equally critical to recognize that tapers also regard the ability to tape music -- whether to preserve it or to make it portable so that it can be enjoyed in a personal or car stereo -- as a key element of the value of the music. Thus, that music can be and is being taped is not to be bemoaned as being detrimental to the industry; instead, it is an essential part of the motivation for purchasing music in the first place.

The relationship between purchasing and taping music is, therefore, synergistic. Tapers are more interested in prerecorded music than nontapers, and, not surprisingly, they spend much more money on music than those who do not tape.[3] Each activity reinforces the other. The words of Rolling Stone magazine of some three years back are as true today as they were then: by taxing tapers, the recording industry is branding "its best customers" -- the "very people" on whom it "depends . . . to turn a release platinum" -- as "its worst enemies."[4]

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[2] Id. at 22, 49, 58. This fact is confirmed by data from surveys commissioned by the recording industry. See, e.g., CBS Records Market Research, "Blank Tape Buyers: Their Attitudes and Impact on Pre-Recorded Music Sales" 12 (Fall 1980); Roper Organization, Inc., "A Study On Tape Recording Practices Among The General Public" 6 (June 1979)("Roper Survey")(tapers' own record and tape collections are "the largest single source" of home recordings).

[3] Yankelovich Survey at 16, 62; Warner Communications, Inc., "A Consumer Survey: Home Taping" 32 (March 1982)("Warner Survey")(only 31% of prerecorded music buyers are tapers, yet tapers account for almost half of the total spent on prerecorded music); Roper Survey at 6-7 (concluding that those who tape are twice as likely to buy LPs and singles as those who do not tape, and four times as likely to purchase prerecorded cassettes).

III. The Recording Industry Fails To Recognize That Home Taping Technology Is Not An Enemy -- But Is One Of Its Greatest Friends

A. The Industry Has Reaped Enormous Economic Rewards From Recording Technologies

The widespread availability of home taping technology has opened multi-billion dollar markets for the recording industry and unparalleled opportunities for the creative community.

The public has embraced recording technology. Sales of prerecorded cassettes now have far surpassed those of LPs, with music in the cassette format outselling disks two-to-one. The billions of dollars in sales of prerecorded cassettes, or of records that are, in part, bought to to be taped, are ample "bottom line" testament that technology is an ally of artists and record companies.

It is the massive endorsement of recording equipment by tens of millions of American consumers that has laid the foundation for the skyrocketing penetration of playback devices for which ever-increasing amounts of music are being purchased. As Russ Solomon, President of Tower Records, said in an interview last year:

> [I]f you didn't have the home-recording business, you wouldn't have Walkman machines. In other words, the tape technology that came out of the recording machine resulted in the portable playback machine

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[4] *See* "The War Against Home Taping," *Rolling Stone*, Sept. 16, 1982, at 59, 64.

> and the automobile machine, which created an enormous market for us.[5]

To shun technological change -- to view it as an enemy that should be subjugated economically to the interests of copyright owners -- defies economic reality and common sense. Copyright owners historically have been all-too dismissive of the benefits that they realize from the creative efforts of others, who invent, produce, and market the equipment and other products that create or expand markets for sound recordings or audiovisual works.[6]

B. Much Home Taping Is Caused By Record Company Reluctance To Adapt To Technological Changes And Consumer Preferences

The recording industry is no exception to the general principle that copyright owners are slow to recognize the benefits that technology can bring.

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[5] M. Goldberg, "The Wisdom of Solomon," Rolling Stone, Nov. 22, 1984, at 39.

[6] The motion picture industry, for example, reacted adversely to the advent of broadcast television, cable television, pay television, and videocassette recorders. Together, of course, these technological developments have created enormously lucrative "ancillary" markets that, in the estimates of some, will contribute nearly 50% to industry revenues in the next few years. *See*, *e.g.*, R. Simon, "The Movie Industry: The Big Picture" 2 (Goldman Sachs Research: Mar. 1, 1984)(box office revenues may account for only 55% of revenue flow by 1988). In fact, home video technology has turned old film vaults into gold mines and has created a revenue stream for new movies that is "literally causing films to be made." T. Seidman, "Blay Sees $2 Billion Year For Video," Billboard, Dec. 22, 1984, at 5, 77 (quoting Andre Blay, president, Embassy Home Entertainment). *See* "Videotapes Give Hollywood A Second Shot at Success," U.S. News & World Report, Mar. 4, 1985, at 73 (Ed Cooper, head of international distribution for Orion Entertainment Group, commenting that Orion is "more money than we ever dreamed of from large libraries").

Beginning in the late 1970s, consumers wanted portability, convenience, and high quality in their music. They realized the advantages of cassette technology in giving them what they wanted and so the public began purchasing car stereos, portable stereos, and "walkman"-type players.[7] The record companies, however, long after consumer preferences had changed, were still turning out LPs and other "black vinyl" product. It came, then, as no surprise to anyone but the record companies, that industry sales and profits slumped in the early 1980's: record companies simply were not making what consumers demanded.

Even today, the recording industry has yet to embrace fully the many opportunities created by the technological revolution.[8] Prerecorded cassettes are still, for some music, harder for consumers to obtain than records. They are not, in many cases, released simultaneously with LPs. Record companies persist in using poor quality tapes, recorded at high speeds, and with shorter playing times for the distribution of prerecorded music on cassettes.

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[7] Sales of portable audio tape equipment more than doubled between 1979 and 1984. Sales have risen annually, from 11.8 million units in 1979 to nearly 27 million units in 1984, with a total projected to approach 29 million units by the end of 1985. Electronic Indus. Ass'n, Consumer Electronics U.S. Sales by Product Category, Table 18, Total Portable Audio Tape Equipment (June 1985). There have been even sharper increases in sales of cassette tape players for automobiles; these increased nearly threefold from 1977 to 1981 (from 3.7 million units in 1977 to 9.7 million units in 1981), and sales have grown from $2 billion in 1981 to a projected $2.8 billion in 1985. Id., Table 21, Total Car Audio Equipment.

[8] The industry's reluctance to perceive and seize technological opportunities is readily apparent in its reaction to the compact disc ("CD") phenomenon. The demand for CD players is exploding, with CDs now the fastest growing configuration in the industry. The new technology has the potential for making substantial contributions to industry bottom lines by making it possible for record companies to sell music on cassettes, phonorecords, and discs. Nevertheless, there are significant shortages of CDs and the industry has moved slowly to release new and old recordings in that format.

Tapers have, therefore, been forced to turn to home taping to obtain the qualities that they cannot otherwise get in the marketplace. Home-recorded tapes can have longer playing times or may be made of tape of better quality than that used by the record companies for prerecorded cassettes.[9] Tapers archive their records, to preserve the music that they own and to listen to it without the wear and tear inherent in repeated phonorecord playback.[10] Tapers want to take high-quality sound with them when they jog, lie on the beach, or drive to work.[11]

Contrary to the cries of copyright owners, then, home taping technology is extraordinarily beneficial to the recording industry. No compensation in the form of royalty taxes should be extracted either from those who developed that technology or from home tapers.

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[9] Tapers regard as "very important" the longer playing time of home-recorded tapes (51% of all home tapers), the better quality of home-recorded tapes (33%), or the durability of home-recorded tapes (31%) as reasons for preferring home-recorded to prerecorded tapes. Yankelovich Survey at 19, 90.

[10] _Id_. at 80 (47% regard ease of damage to records as a "very important" reason for preferring home-recorded tapes to records).

[11] Portability of music is "very important" to 75% of those who tape; indeed, half of the time spent listening to home-recorded music is spent listening on portable systems -- where records are not practical. _Id_. at 18, 80.

Such pleas for compensation are even less seemly when it is evident that the industry's very own lethargy or myopia with respect to technology has been a major impetus for home taping behavior. Viewed in this broader context, to propose that a royalty tax ought to be paid to record companies is wholly unjustified.

IV. The Recording Industry's Economic Recovery Undercuts Its Claim For Compensation From Home Taping Activity

The hollowness of the recording industry's clamor for legislative relief is underscored by its record profits and sales in 1983, 1984, and, now, 1985. Although record companies have been arguing for over four years that a royalty tax is justified because sales of prerecorded music should have been higher in the late 1970s and early 1980s, the current boom demonstrates what everyone else has long realized: home taping is nothing but a convenient scapegoat.

A. These Are The Industry's Best Years Ever

Last year the recording industry had its best year ever, with revenues rising 15% to $4.37 billion, exceeding the previous record, set in 1978, of $4.13 billion.[12] In 1984, virtually every company had a banner year of profits and revenues.[13] The performance of the industry in 1985 is outpacing the record rates of 1984, with gains at retail in the first half of the year of as much as 20% over 1984.[14] The industry has totally recovered from its downturn of some years back. No legislative relief is necessary for an industry that is, by all accounts, doing just fine.

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[12] See "Disk Industry Volume Up 15% For '84; Cassettes Are The Key," Variety, Apr. 10, 1985, at 87; I. Horowitz, "'84 A Peak Year for Recordings: Industry Net Shipments Worth $4.5 Billion," Billboard, Mar. 23, 1985, at 1.

B. The Industry's Past Problems Had Little To Do With Home Taping

That home taping was merely a scapegoat was noted at the time by some record company executives and industry observers.[15] Today, the facts demonstrate that these critics within the recording industry -- as contrasted with the industry's lobbyists -- were right. Some of the causes for the slump -- and for the recovery -- admittedly were beyond the immediate control of the industry. As the economy improved, it carried sales of prerecorded music along with it. The videogame fad, which had siphoned billions in disposable income, ended.

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[13] CBS Records Group led the way with an all-time high of $1.27 billion in sales, representing a 9% increase in revenues. "A Year for Records," Fortune, Apr. 1, 1985, at 10. RCA reported a 4% gain in worldwide record sales, to $621.8 million. I. Lichtman, "RCA Records Posts '84 Sales Jump," Billboard, Mar. 23, 1985, at 4. Warner Communications' Music Group revenues climbed 7%, to $817.57 million, with operating income soaring 32%, in what was described as the "biggest year ever." "WCI Music Group Posts Boffo Results for 1984, 4th Qtr.," Variety, Feb. 20, 1985, at 73; S. Sutherland, "Warner Bros. Music: 'Biggest Year Ever,'" Billboard, Mar. 16, 1985, at 6.

[14] J. Sippel, "CD, Video Contribute to Strong First Half," Billboard, July 13, 1985, at 1.

[15] At the time, Russ Solomon of Tower Records termed home taping and record rentals as "the excuses that record executives and media mavens have offered to describe our long-rumored demise." "Solomon's Wisdom: Music Is Power," Billboard, Apr. 23, 1983, at 4.

Other factors contributing to the downturn were very much the result of industry marketing failures. The industry had been slow to adjust to the demand for portability and convenience. As it began to do so, however, markets created by new products, such as the Walkman and the "boombox," boosted record company sales of prerecorded cassettes. In 1984, cassettes overtook albums as the preferred format, with the dollar value of cassette shipments representing over 55% of the industry's total revenues.[16]

The industry also began applying some sound principles of financial management to its operations. It began cutting costs, ending some of the extravagant practices of the late 1970s. The industry increased cash flow, by adopting new payment and "returns" policies; these policies have, however, while bolstering industry "bottom lines," also had the effect of hampering retailer flexibility to market aggressively. The industry also reduced staff and tightened artist rosters by moving cautiously on signing new artists and letting go older, marginal acts.

These efforts at financial consolidation bear further discussion because the music industry is blaming home taping for the recent decrease in new releases. In light of the record high revenues in 1984, the decision to reduce the number of new releases cannot be based on low industry coffers but rather, I suspect, reflects an internal business judgment by industry executives that it is more profitable for them to place greater emphasis on fewer acts.[17] It is inconceivable that the record companies would revert to their less efficient and less profitable approach, even if they received more money from consumers. Taping is not the real reason for fewer releases and the tax will not necessarily increase releases at all.

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[16] "Disk Industry Volume Up 15% For '84; Cassettes Are The Key," Variety, Apr. 10, 1985, at 87; "RIAA Figures: Cassettes Paced A Record '84," Billboard, Apr. 13, 1985, at 1.

At the same time as the industry began adopting these new efficiency measures, it also began to sell the stars it retained. It is hard, indeed, to blame home taping for imagined record company ills when last year saw the release of multi-million seller "mega-albums" by Michael Jackson, Bruce Springsteen, Prince, Lionel Richie, and Chicago. Such phenomenal success belies the industry's argument that home taping practices have made it difficult to make a profit at the top end of the market. Michael Jackson's "Thriller" album is the biggest seller of all time -- and how necessary is a royalty tax to stimulate creativity when he made $70 million from the sales of that album?

The industry also began promoting its music in ways that aroused public interest. The use of music video has been the major engine of the industry successes of the '80s. Whether on music video television programs, through video clip "tours," or by cross-promoting with prerecorded videocassettes, the record companies are finally starting to use some of the technologies that are changing, and benefitting, the industry. At the same time, radio airplay, the traditional promotional tool, has been reinvigorated by video promotion.

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[17] See P. DiMauro, "Disk Labels Play Cautious Game, Once Burned, Twice Shy On Signing," Variety, Feb. 13, 1985, at 1.

Three years ago Congress was right to recognize the unfairness of enacting a legislative cure for ailments that were largely of the industry's own making. Confronted with problems and having had its pleas for a bail-out rejected by Congress, the industry was forced to develop and apply its own corrective measures. And those steps have made a difference, contributing significantly to the phenomenal success of the last couple of years. Now, faced with pleas from an industry that has never been healthier, there is even less reason than before for Congress to saddle millions of American consumers with the costs of a federal hand-out.

V. Royalty Taxes Are Unwarranted And Would Provide An Unjustified Windfall For The Recording Industry

A. Most Home Taping Activities Are Not Of The Type Complained Of By The Recording Industry And Others Actually Stimulate Sales Of Prerecorded Music

Against the backdrop of the economic realities of the recording industry, and with an understanding of how home taping has been used as a scapegoat by proponents of a royalty tax, it is important to return to a fundamental proposition. That is, a home-recorded tape does not equal the lost sale of a prerecorded album or cassette. Rather, "home taping" describes a set of different and interrelated activities, each of which has its own economic consequences.

First, a great deal of home taping, over half, according to the results of the Yankelovich Survey, does not involve prerecorded music.[18] People tape their own performances of music, dictation, telephone messages, family occasions, language or music lessons, rehearsals, lectures, letters to relatives, bird calls, computer programs, along with literally hundreds of other sounds. No compensation is owed to record companies, nor should any be imposed, for all these kinds of taping.

Moreover, the recording industry argument that home-recorded tapes displace sales of prerecorded music is difficult to square with actual home taping activity. Home-recorded tapes that do contain music are not simple substitutes for prerecorded music. By far, the most common home music taping activity is putting together musical selections for a customized home-recorded tape.[19] Such tapes are, by definition, unavailable on the marketplace: when they are made, there is no displacement. At the same time, the demand for particular songs desired for a selection tape can stimulate -- not impair -- sales of prerecorded music.

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[18] Yankelovich Survey at 18, 36-39 (52%). Even the Roper Survey, conducted for the recording industry, found that 31% of all blank tapes were never used for recording music. Roper Survey at 11. The survey conducted for the recording industry by Audits & Surveys calculated the percentage of tapes containing "music" (84%) -- a figure that includes all music, and not just that which is "prerecorded." Audits & Surveys, "Home Taping in America: 1983, Extent and Impact" 10 (Oct. 1983). The Audits & Surveys report itself, moreover, acknowledges that an alternative method of calculation shows that up to 35% of home taping involved non-copyrighted material. The accompanying industry caveat, that this method does not take into account possible reuse of tapes, itself eviscerates the argument that taping displaces purchase.

[19] The findings of the Yankelovich Survey demonstrate that the most common reason -- cited by 72% of respondents as "very important" -- for home taping was to put together selection tapes. Yankelovich Survey at 3, 17, 65. Two-thirds of their collections contained only musical selections. Id. Nearly half reported that fewer than 20% of the tapes they had made included a complete album. Id. at 65. The Warner Survey report expresses "surprise" at the amount of selection taping, and concludes that 45% of taped units are of "selection albums." Warner Survey at 20.

B. Royalty Taxes Would Constitute Double Payment To Copyright Owners

A royalty tax would force home tapers to pay a second time for their use of prerecorded music. When consumers buy prerecorded music they are not just purchasing a piece of vinyl or some magnetic tape in a shell. They purchase the right to enjoy the music. When they tape that music, for their car, their portable stereo, or at the office, they are simply extending the area in which they can enjoy what they have bought.

As noted previously, the surveys are unanimous in agreeing that most home music taping is from tapers' own collections.[20] Such taping is simply an enhancement of prerecorded music for which the purchase price (including a royalty) has already been paid to the copyright owner.

Taxing the predominant home music taping activity -- taping by individuals of music in their own collections -- implies that music lovers should be forced to buy multiple copies of the same music or be economically constrained from making customized compilations of material in their own collections. Thus, unless the recording industry is contending that music can only be enjoyed by consumers in one location and at one time, or that consumers should be penalized for home taping, a royalty tax constitutes unwarranted double compensation for copyright owners.

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[20] Yankelovich Survey at 22, 54 (51% of all home music tapes); Warner Survey at 22 (45% of music tapes); Roper Survey at 6 (37% of everything taped). The Audits & Surveys report, however, refused to release data as to who owned the records and prerecorded tapes that it claims were taped.

Even as to the borrowing and taping of prerecorded material, it is far from clear that that activity should be taxed. Sharing belongings with friends or within a family is an ordinary part of human conduct. With respect to copyrighted material, such as books and records, copyright law recognizes the importance of exchanging and disseminating works. Indeed, the law contemplates that the ability to share prerecorded music is an element of the price that is paid to copyright owners. With respect to music, it is only natural that friends or relatives want to share what they own and enjoy. Taping may also occur because record owners want to ensure proper handling of records in their collections.

In deciding whether additional compensation should be coerced from individuals who engage in such normal social interaction, it is important to note that lending and borrowing does stimulate interest in the album or music of the artist that was exchanged. In some instances, moreover, friends may pool resources to buy, and share, an album or cassette that, on their own, none could afford to buy. In short, royalty tax payments to record companies should be rejected because it is clear that, for most home taping activity, 1) there has been a purchase of prerecorded music and 2) there has been or will be no displacement of sales of prerecorded music.

VI. S. 1739 Is Overbroad, Arbitrary, And Unworkable: It Will Distort Technology And Alter The Existing Balance Between The Technological And Artistic Communities

The proposal to tax audio recorders and tape, S. 1739, has a number of flaws that are irremediable: 1) the tax is overbroad and would tax all uses of audio recorders and tape; 2) the level of the tax is arbitrary; 3) taxing recording equipment and media will inevitably distort technological development; 4) the proposal uses a mechanism for distribution that cannot carry out the task in a way that will generate incentives for creators; and 5) in direct contravention of the Supreme Court holding in Sony v. Universal City Studios, the legislation grossly expands the concept of contributory infringement.

A. The Tax Is Unfairly Overbroad

Regardless of whether a purchaser of audio equipment or tape uses them to record copyrighted music, he or she would be forced to pay a royalty tax. Such a tax is particularly unfair for those who never or seldom use their recorders to tape prerecorded music.[21]

Recognizing the obvious unfairness of such a tax, the industry proposal uses a surrogate for actual use -- types of tape -- in an attempt to exempt certain users from paying the record companies. Conferring authority on the Copyright Royalty Tribunal to exempt products that are not "suitable" for taping copyrighted material is, however, no solution to the overbreadth problems of S. 1739.

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[21] According to the Yankelovich Survey, 23% of all tapers have never taped prerecorded music. Yankelovich Survey at 15. Even the recording industry-sponsored Warner Survey finds that 9% of all tapers have never taped music. Warner Survey at 12.

First, as Len Feldman will explain in greater detail, it is technically impossible to segregate tape by type. This Subcommittee heard testimony in October 1983 that tapes cannot be categorized by their purported lack of "suitability" for the taping of music.[22] Nothing has changed since that time. The decision to use a particular kind of tape depends on individual economic resources, the importance ascribed by the taper to high fidelity, the need to preserve data, the hardware available, or a myriad of other factors. The simple truth is that people use all kinds of tape and equipment to tape all kinds of sounds.

Furthermore, the "exemption" provisions of the recording industry proposal are imprecise and inequitable and, consequently, likely to result in abuse. They would impose taxes on machines that could be used for taping prerecorded music, but seldom or never are. Although S. 1739 purports to require the CRT to "exempt" classes of users who use recorders and tapes for business, the proposal is flawed. Many users, equally as deserving as those that the bill would purportedly "exempt," would not be exempted.[23] There is no way around the fact that the bill -- and any taping tax -- would discriminate against a large class of individual purchasers of equipment who do not engage in "home" taping.

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[22] See Video and Audio Home Taping: Hearings on S. 31 and S. 175 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. 443 (1983) (statement of Edward J. Foster, Diversified Science Laboratories) [hereinafter "Video and Audio Home Taping"].

[23] Although the bill would exempt businesses invoking Internal Revenue Code sections 162 and 167, it would, for example, tax tape and recorders bought with a profit-seeking purpose, and, therefore, deductible under section 212 (permitting deduction of "ordinary and necessary business expenses . . . for the production or collection of income").

Without describing in detail the nightmares presented by administration of the "exemption" provisions, it is clear that they are shams. Not only will they not work in practice, it is probable that they are not even meant to do so. Indeed, the problems with handling the literally millions of annual claims for exemption, reimbursements, and, possibly, a dual inventory scheme of "taxed" and "untaxed" products are so massive that they do nothing toward solving the problems of overbreadth. The exemption provisions, in short, are entirely unworkable; nevertheless, no system is fair without providing for an exemption. The only solution is no tax at all.

B. The Proposed Amount Of The Tax Is Arbitrary

Although the intent of the royalty tax legislation is to compensate copyright owners for any "losses" from home taping, the amount of the levy -- 5% on audio recorders; 25% on dual cassette recorders; a penny per minute on blank tape -- is simply pulled out of thin air. There have been no comprehensive studies of the overall, net financial impact of home taping on copyright owners. It is not surprising, therefore, that the only relationship between the amount proposed by S. 1739 and either the amount of home taping or the level of any purported damage from taping practices is an arbitrary one.[24]

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[24] There is little comfort in the provisions that authorize the CRT to "adjust" the amounts of the

C. A Royalty Tax Will Distort Technology

Imposing a royalty on some products, but leaving others untaxed, will significantly intrude on technological decisions about the future course of consumer electronics technology that are best made in the marketplace. Manufacturers will have substantial incentives to reconfigure products to avoid the levy. At the least, to satisfy consumer demand, they may be inclined to move the taxable recording components into separate, low-cost, units to maintain lower prices.

More dangerously, subsequent developments will be skewed by, or overtake, any classification schemes that focus on technology at a single point in time. It is difficult now and will become impossible in the future to make the neat classifications that the proponents of S. 1739 would prefer. For example, videocassette recorders are used to make high-quality, long-playing sound recordings. Video and audio technologies are fusing in the new eight millimeter standard. Stereo sound is becoming a standard element of television broadcasts and prerecorded videocassettes.

Yet, the proposal contemplates that the CRT will consider regulations that would impose a tax on "suitable" technology. Decisions to tax videorecorders under S. 1739, or spending an extended period of time in resolving the issue of whether video and mixed

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(footnote continued)

statutory levy, given the agency's lack of resources and its lack of expertise in audio recording technologies. Moreover, the burdensome impact of the tax will be felt by consumers and will affect technological developments for the five years prior to the first time that the CRT would be authorized to make any such adjustments.

audio/video equipment is covered by the bill, will inhibit innovation in consumer electronics.

More broadly, the ongoing task of analyzing developments, continually classifying new products, and conducting searching examination of the technological marketplace is government intervention with a vengeance. Manufacturers will be required to submit to the CRT proprietary information about the characteristics of new tape and recording equipment products. It may be difficult to provide adequate safeguards against disclosure of such commercially sensitive information.

One result of the proposed exemption scheme, therefore, may be to force proprietary product information into the public domain, with the serious consequence of impairing the competitive relationships that now characterize the tape and equipment market. In sum, governmental oversight of the process of developing new consumer electronics products, as required by the royalty tax proposals, would be intrusive and likely to stultify competition and new entrepreneurial activity.

D. The Distribution Mechanism Is Unworkable And Will Not Provide Incentives For Creators

The mechanism for distributing funds is fundamentally flawed because the CRT, the agency with the responsibility for disbursing the royalty proceeds to copyright owners, is beset with problems.[25] The CRT is now in danger of being disbanded due to problems that include its inadequate staffing and its approach to the tasks with which it is charged under the copyright law.[26] Two bills have been introduced in this session of Congress to overhaul it.[27] The experience to date with the CRT has shown, repeatedly and consistently, that it simply does not have the continuity, expertise, and coherence to perform the distribution function.[28]

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[25] These problems were noted in my testimony of October 1983, in which I recounted how both former CRT Chairman Clarence L. James, Jr. and Jack Valenti of the Motion Picture Association of America called for the agency's abolition. See Video and Audio Home Taping, supra note 22, at 375 (statement of Charles D. Ferris).

The distribution procedure gives prominent play to claimant negotiations that might culminate in a voluntary agreement regarding the distribution of the royalty fees. The hope that such agreement can be reached is nothing more than wishful thinking. The number of claimants involved,[29] the absence of any agreed methodology for measuring the amount of home taping either in the aggregate or for particular songs,[30] the bill's utter lack of any criteria to guide the distribution process, and the consistently contentious character of all other proceedings before the CRT all leave little room for optimism that the claimants would or could resolve their differences expeditiously.

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[26] That the CRT's resources are inadequate has been the subject of much judicial notice in the context of the repeated appellate proceedings that have challenged the Tribunal's determinations. See National Ass'n of Broadcasters v. Copyright Royalty Tribunal, No. 84-1230, slip op. at n.9 (D.C. Cir. Aug. 30, 1985); Christian Broadcasting Network, Inc. v. CRT, 720 F.2d 1245, 1304 (D.C. Cir. 1983); National Cable Television Ass'n v. CRT, 689 F.2d 1077, 1087 n.74 (D.C. Cir. 1982).

[27] H.R. 2784, introduced by Rep. Kastenmeier, would establish a new federal Copyright Royalty Court composed of three sitting federal judges appointed for six-year terms, and give it support staff, clerks, and a general counsel. Competing parties would first be required to negotiate among themselves, and to accept intervention from a court-appointed mediator if necessary. If voluntary agreement were not reached, however, the bill is aimed at ensuring that the new court would have expertise both in methodical evidence-gathering procedures and in the substantive law and economics of royalty distributions. H.R. 2752, introduced by Reps. Schroeder and Synar, would abolish the CRT immediately and transfer its duties to the Register of Copyrights pending a more thorough reform.

[28] Empowering the CRT to adjust the amount of the levy and to disburse the proceeds raises a significant concern with respect to the constitutionality of the proposal. Recent decisions of the Supreme Court suggest that such tasks -- adjudicating interests between private parties and involving essentially private rights -- should be undertaken by federal courts, created pursuant to Article III of the Constitution, and not by entities created by Congress pursuant to an exercise of its Article I powers. See Thomas v. Union Carbide Agricultural Prods., Co., 105 S. Ct. 3325 (1985); Northern Pipeline Construction Co. v. Marathon Pipe Line Co., 102 S. Ct. 2858 (1982).

Nevertheless, if copyright owners do not agree as to what each should receive, they will find themselves litigating before the CRT in a proceeding that is bound to be lengthy and intrusive. Moreover, correlating a home taping event and the receipt of compensation will be extraordinarily difficult.[31]

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[29] The number of potential claimants is very large. The bill says that "every person claiming to be entitled to royalty fees" may file to receive part of the distribution. Entitlement hinges on whether a copyrighted work was broadcast or included in a phonorecord distributed to the public during the relevant royalty collection period. Over 20,000 published musical works are copyrighted each year, as are over 10,000 published sound recordings. Copyright Office, Library of Congress. There are, therefore, several hundred thousand copyrighted works for which there could be claims under S. 1739.

[30] Existing mechanisms for distributing performance royalties to the owners of copyrights in musical works -- ASCAP or BMI -- are based on surveys of music broadcast or otherwise publicly performed. Their methodologies could not be adapted without intrusive surveys of the use of music taped in the home, a burden that our rights of privacy could not -- and should not have to -- bear.

The inability to correlate any actual home taping with compensation for it, coupled with the delay in distribution, will create substantial uncertainty for record companies with respect to the receipt of royalties. It will be nearly impossible for them to rely on proceeds from the royalty fund in evaluating the profitability of particular artists or kinds of music. The royalty tax proceeds, therefore, will not serve their intended purpose -- as an incentive for the creation of copyrighted works demanded by the public.

E. Enactment Of An Expanded Concept Of Contributory Infringement Will Confer On The Recording Industry Unwarranted Power Over The Electronics Industry

S. 1739 deceptively grants consumers a home taping "exemption" while forcing them to pay a new tax for engaging in practices that the bill ostensibly legitimates. Congress should be aware, however, that by codifying the concept of contributory infringement it is enacting legislation that is directly at odds with the Supreme Court approach of the Sony decision. More fundamentally, the contributory infringement sections of the bill would accord the recording industry nearly unconstrained new power to seek relief from equipment and tape manufacturers.[32]

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[31] Only surrogate measures, at best, for the incidence of home taping will be available. Such measures, which might includes sales of prerecorded music, radio and television airplay, surveys of home tape collections, press coverage, and other data will take a long time to collect. Claimants before the CRT are likely to complicate the process by stressing factors most favorable to their own claims.

At the heart of the recording industry proposal is the notion that manufacturers should be liable for how the public uses their products. With respect to home taping, it circumvents the Supreme Court holding in Sony by making manufacturers and importers liable for home taping -- a liability not now imposed by the law. By invoking this provision, copyright owners would have plenary power over product development in the electronics industry, completely tilting the state of market equilibrium between the technological and artistic communities that currently prevails.

* * * * *

The recording industry has been trying for years to cure the defects in its various proposals to tax recording technology and tens of millions of home tapers. It has yet to succeed. The truth is that the industry has done phenomenally well, and home taping has helped it to fabulous successes. The industry's attempts to extract more money from the American public have never been seemly. Today, however, with the industry's own pockets overflowing, there has never been a better time to reject royalty taxes as an idea whose time will never come.

Thank you, Mr. Chairman.

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[32] Proposed Section 119(a) would provide that "nothing in this section shall exempt from liability a person who, for purposes of direct or indirect commercial advantage, induces, causes or materially contributes to the making of audio recordings by any individual or entity."

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December 2, 1985

Honorable Charles McC. Mathias
Chairman
Subcommittee on Patents, Copyrights
and Trademarks
Committee on the Judiciary
United States Senate
137 Dirksen Senate Office Building
Washington, D. C. 20510

Dear Mr. Chairman:

At the October 30, 1985, hearing on S. 1739 before your Subcommittee, George David Weiss and Stanley M. Gortikov contended that the proceeds from the royalty tax would benefit the creative community and, in particular, singers, songwriters and other "struggling artists."

That argument is belied in its entirety by the structure of the music business -- which essentially compensates only the already-wealthy record companies, music publishers or industry superstars. Directly rebutting the music industry's assertions that regulations will ensure that home taping money is directed to creators, the attached paper documents why struggling artists could not and would not benefit under S. 1739.

I would very much appreciate your including this letter and the accompanying paper in the record of the hearing.

Thank you.

Sincerely,

Charlie

Charles D. Ferris
Counsel, Audio Recording
Rights Coalition

CDF:dls
Enclosure
1929f

cc: Steve Metalitz

THE RECORDING INDUSTRY MYTH OF ROYALTY TAX "TRICKLE DOWN": THE TRUTH ABOUT PAYMENTS TO STRUGGLING ARTISTS

I. Introduction

This paper describes the structure of the recording industry and how artists receive payments for their creative works. It is submitted by the Audio Recording Rights Coalition to demonstrate the utter fallacy of the proposition -- put forth by the recording industry -- that S. 1739 would benefit struggling artists. Seeking to exploit legitimate congressional sentiment in favor of increasing artistic creativity, the recording industry argued before this Subcommittee on October 30, 1985,[1] that the proceeds from a consumer-paid home taping levy would flow directly to creators and, in particular, to artists such as songwriters, instrumentalists, and vocalists.

The facts, however, rather starkly contradict the industry's arguments. Little, if any, royalty tax money would reach any creative artist. The "struggling artist" argument, then, not only should not be a basis upon which Congress can enact S. 1739 or any other royalty tax legislation, but also, all too clearly underscores the industry's greed in persuading lawmakers that its own coffers should be engorged.

II. Summary of Argument

One element of the recording industry's case for a royalty tax on audio tape and recording equipment is the argument that home taping levies will further the purposes of the copyright law by somehow benefiting struggling artists.[2] Although that argument plays on emotional attachments to the artistic community, it is completely unsupported by the facts -- which demonstrate that the scheme by which the music business compensates virtually all singers, instrumentalists, and songwriters makes it improbable that anything but essentially insignificant monies would ever be seen by creators.

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[1] *See* Joint Statement of National Music Publishers' Association, Inc., Recording Industry Association of America, Inc., and Songwriters Guild of America, Re: S. 1739, The Home Audio Recording Act, Before the Subcommittee on Patents, Copyrights and Trademarks of the Senate Committee on the Judiciary, 83-85 (Oct. 30, 1985).

First, the legislative proposals would distribute the proceeds from the royalty tax to the owners of copyrights in sound recordings and musical works. Who owns these copyrights? Copyrights in sound recordings are nearly always held by the record companies. Copyrights in songs are owned in most cases by music publishers. Performers -- bands, orchestras, singers, and instrumentalists -- own nothing and would get no money by the terms of S. 1739.

Thus, for songwriters and performers to get any portion of the royalty tax proceeds, they will have to bargain with record companies and music publishing houses. Distribution to creators will depend on the contractual arrangements they have managed to reach and on industry "generosity," not on any statutory mandate.

Little in the history of the industry's dealings with artists or in its traditional compensation structure suggests that it will be generous. Longstanding industry practice is for record companies and music publishers to pay most artists -- save only the few, already well-compensated superstars -- only a very small fraction of the total royalties that are received. The payout is reduced further by the standard industry practice of deducting from an artist's royalty account all or part of the cost of producing and promoting songs and recordings. A fair picture of how the industry operates, therefore, is that the powerful companies leave the relatively powerless artists with only a minute portion of overall revenues.

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[2] Before Congress are two bills that would impose such a tax. S. 1739, 99th Cong., 1st Sess. (1985); H.R. 2911, 99th Cong., 1st Sess. (1985).

There is, then, no reason to believe that any new revenues, from a royalty pool, would be passed on to struggling artists in anything more than token amounts. If there is an interest in helping artists, whose cause is championed so vigorously by the industry, Congress might well focus its energies on the size of current industry payments to those who are "struggling." An industry that were truly committed to helping these artists would be directing some of the tremendous revenues that it is now enjoying to young and less popular singers and songwriters. To the contrary, the industry's record belies its newly-found concern for struggling artists.

In short, by taxing consumers to create a royalty fund of hundreds of millions of dollars, Congress would only be enriching the corporate treasuries of record companies and music publishers, and not supplementing the income of struggling artists. At best, royalty taxes could add to the vast earnings of the industry's superstars. These artists, however, need no further incentives -- beyond those already provided by the marketplace -- to produce creative works. Thus, the goals underlying the copyright law would not be served by exacting additional copyright dollars from consumers in the form of a royalty tax.

III. Ownership of Copyrights In the Recording Industry

The appealing notion that a tax on audio tape and recording equipment will assist the nation's struggling artists is, to put it bluntly, a fallacy. First, as to any "struggling" performers, they are, quite simply, unrecognized in the copyright law. Second, most composers and lyricists do not own the copyrights in the musical works they compose or write. In the music business, an industry where a multitude of creative individuals are vying for the financial backing of a relatively small number of companies, the price of a chance for success is extremely high. The cost to the artist typically is the assignment of ownership and control of his or her creative works. The structure of copyright ownership means that royalty tax legislation primarily will reward the already prosperous record companies and music publishing houses -- and not the real creators of our nation's music.

A. Copyrights in Sound Recordings

Record companies, in virtually all cases, own the copyrights in sound recordings. As a result, these record companies, not performers or songwriters, would receive monies that S. 1739 would pay out to the owners of the copyrights in the works embodied in phonorecords and tapes.[3]

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[3] See H.R. 2911, 99th Cong., 1st Sess. § 2(b)(4) (1985) and S. 1739, 99th Cong., 1st Sess. § 2(b)(4) (1985) (both providing that fees on cassettes and recording equipment "shall . . . be distributed to the owners of copyrights in musical works and sound recordings").

There is, of course, nothing inherent in the concept of copyright or in copyright law that states that the record companies must own or are entitled to the copyrights in sound recordings. Indeed, for many years there was no copyright in sound recordings. And, in 1971, when Congress first accorded rights to the producers of sound recordings,[4] it recognized the limited creative contributions made by producers -- those who bring together the songs, the performers, the engineers, and the marketing expertise, and distribution mechanisms.[5]

It is possible for a name "performer" to act as a producer and own the copyright in the composite work -- the sound recording. Given industry structural arrangements and some disinterest by the creative community in distribution and marketing, performer ownership of sound recordings is so rare (even in the case of superstars) as to be essentially nonexistent.

In short, then, to "win" a recording contract, a performer ordinarily must agree that the record company will own all rights to the composite work that emerges from a production session -- i.e., that it will own master recordings or other tapes containing sound recordings.[6] Typically, both established performers and new artists must consent to this allocation of rights. This ownership arrangement is a result of a business in which a very large number of potential artists must seek the services of a very small number of successful record companies.[7] As it is these mega-companies that would benefit from a royalty tax, there is no surprise that these same companies are leading the charge in support of S. 1739.

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[4] Sound Recording Amendment of 1971, Pub. L. No. 92-140, 85 Stat. 391. The 1971 Act has been recodified by the 1976 Act in 17 U.S.C. §§ 114 & 301(c).

[5] It is clear that Congress recognized -- and continues to recognizs -- that the producer of a sound recording makes minimal contributions to the creative efforts of the songwriter. It took several decades for there to be any recognition that sound recordings -- as a product distinct from the musical works that they embodied -- were entitled to copyrightability. Moreover, sound recording copyrights still have a second-class status, with their owners vested with the exclusive rights of reproduction, preparation of derivative works, and distribution, and not -- unlike other works (e.g., musical or literary works) -- with the right of public performance. See 17 U.S.C. § 114(a).

Given that the record companies own the rights in sound recordings, for an artist to receive any portion of the revenues from the sale or use of such recordings, the record company must agree either to transfer ownership of the copyrights to the performer or to make specific payments to the artist.[8]

There is no reason, however, to expect that record companies, in the future, suddenly will decide to transfer copyrights to any performers or songwriters, whether struggling or not Even particularly famous, and, therefore, powerful, performers have a difficult time in owning the copyrights in recordings they have made; occasionally, they are able to negotiate for reversionary interests in the copyrights in certain sound recordings.[9] Record companies still, typically, retain the right to receive the royalties from the initial -- and probably most substantial -- portion of a "hot" artist's record sales.

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[6] See S. Shemel & M. W. Krasilovsky, This Business of Music 10-11 (4th ed. 1979) [hereinafter cited as Shemel & Krasilovsky].

[7] Six companies, through distribution agreements, control more than 80% of the market. Warner, CBS Records, RCA, MCA, EMI-America, and Polygram own more than fifteen major record labels, which account for an overwhelming majority of the current record sales. See infra, note 22.

In 1984, the Federal Trade Commission reacted to this oligopolistic market structure by moving to block a proposed merger between Warner and Polygram. As a result of the challenge, the merger plan was dropped. See generally Landro, Merger of Warner Unit, Polygram Angers Troubled Record Industry, Wall Street Journal, Apr. 12, 1984, at 33.

[8] Such payments, which are negotiated as part of a recording contract, are considered below in Section IV.

Without owning the copyrights in sound recordings, a record company might find itself unable to exploit individual recordings -- which it might want to do as, perhaps, part of an anthology or as a late release that capitalizes on a performer's belated fame. Ownership of the copyrights in sound recordings provides the record companies with the maximum opportunity to profit from the artists whose works they buy.

S. 1739 actually might increase the reluctance of record companies to give creators any copyright interests in sound recordings. By making these interests potentially more lucrative, the proposed legislation would increase the amount of money that a record company could lose by giving up a copyright interest. Business sense alone, therefore, suggests that these companies will make every effort to retain ownership of the sound recording copyright.

B. Copyrights in Musical Compositions

Although S. 1739 also would distribute proceeds from the royalty tax to the owners of copyrights in musical works,[10] it is once again true that the artists -- in this case the composers and lyricists who created the works -- typically do not own such copyrights. Consequently, S. 1739 would confer no benefits directly on the songwriters.

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[9] See Shemel & Krasilovsky, supra note 6, at 11.

[10] See supra note 3.

The composer of a song generally must rely on a music publishing house to market musical compositions.[11] These publishers exact a huge fee -- usually 50% of all royalties received -- for services that may not even include a guarantee of or any other arrangements for actually recording the song.

In many instances, the publishing houses assume ownership of the copyrights in original songs for a minimum of 28-35 years. Publishers frequently contend that they should be entitled to the full term of the copyrights in songs.[12] Thus, they seek to gain ownership of this full term during negotiations with writers.[13] Even where writers retain a recapture right after the minimum period, either because they are famous enough to have a strong negotiating position or because they are protected by the American Guild of Authors and Composers contract, the publisher would control the copyrights for what are likely to be a song's most lucrative years.

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[11] There are some rare instances where a songwriter is able to bypass a music publisher and market a song directly to a star recording artist.

[12] In compositions subject to the Copyright Act of 1909, the original term of the copyright was 28 years. A renewal term of 28 years also was available. Under the 1976 Act, this term has been changed so that works not published or copyrighted before 1978 are protected for the life of the author plus 50 years. The 1976 Act also extended the copyright protection for works that were in their original or renewal terms in 1978.

The American Guild of Authors and Composers (the "AGAC"), the dominant songwriters union, has entered into agreements with many publishing houses that obligates them to use a standard AGAC contract when dealing with member writers. Under this contract, the publishing houses are now entitled to the copyrights in original compositions for a term not to exceed 40 years. See Shemel & Krasilovsky, supra note 6, at 144-45, 527-39 (Form 1).

[13] Shemel & Krasilovsky, supra note 6, at 145.

Pursuant to contractual agreements between the writer and the publishing house, writers typically receive something less than half of the royalties collected by the publishers under the copyrights. These sums are offset by various other payments and expenses, as is discussed below in Section IV.B. The simple truth is that lyricists and composers get little -- and music publishers benefit greatly -- from the current system.

Given the minimal services and high fees that characterize the music publishing business, some creative writers and composers with marketplace power have sought to avoid the music publishers' middleman "bite." Such artists may form their own publishing houses so that they can retain ownership of the copyright in the songs they write and can collect the full royalty.[14] Of course, only the industry's superstars enjoy the luxury of their own publishing houses, and it is these stars who would get the lion's share of any royalty tax proceeds.

When songwriters assign copyrights in their compositions to music publishers, they expect the publisher to use its best efforts to exploit the work by publishing it in sheet music form, obtaining an agreement to record the work, or licensing the composition for use in a television program or motion picture.[15] As a result of this ownership arrangement, publishers have exclusive control over all decisions about the mechanical reproduction (recording), printing, and other licensable uses of a musical composition.[16] As virtually all elements relative to the success of a particular song are left to the publisher, once the writer has composed the song, subsequent financial reward is essentially not within his or her control.

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[14] The Beatles, for example, owned the copyrights to their own songs for just such a purpose. The Beatles sold those rights in the late 1960's, and they came to be owned by ATV Music. It was ATV Music that was purchased in mid-1985 by Michael Jackson for $45 million. See Jackson's Buyout of ATV Receives Little U.K. Notice, Billboard, Aug. 31, 1985, at 8. That the creative contributions of music publishers are minimal, at best, is emphasized by the fact that it is Michael Jackson who will gain from continued sales and airplay of Beatles songs -- and not the creative artists themselves.

The structure of the music publishing business, then, results in an incredible windfall for publishers. A publishing house that makes a song available to a performer or record company can collect on the future success of that song without ever having to work toward ensuring its success. If the song does well and receives airplay time, other musicians will decide to record the song. Their decisions will be based on having heard the song on radio or television, not on any creative effort on the part of the song's publisher. Each time the song is recorded -- after the first recording -- the music publisher can simply sit back and collect mechanical royalties -- the compulsory license fee that must be paid for the right to record that song.[17]

What does the writer get for composing the song? Maybe half of the royalty payments -- or less, depending upon individual contract arrangements. The publisher will get an equal or greater share! This business is so lucrative that the owner of one New York publishing house, Chappell & Co., confessed that "you can't lose money" and that "it's the most unbelievable business."[18]

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[15] Shemel & Krasilovsky, supra note 6, at 148.

[16] In some cases, a writer may have a contractual right to recapture the copyright in a composition if the publisher fails to exploit the work to the writer's satisfaction.

[17] See infra, Section IV.B.

Yet, in lieu of compensating creators, S. 1739 only would pay more money to these publishing houses. Nevertheless, as the recording industry has argued consistently in opposing any increases in the compulsory license fee that it must pay to publishers,[19] publishers already are extremely prosperous. Absent a contractual commitment by the publishers to pass along this increase to writers, neither struggling nor successful composers and lyricists would see any money from the taping tax. And, of course, songwriters wealthy enough to set up publishing houses for their own music need no additional money to motivate their creative efforts.

In sum, the copyright-based compensation mechanism of S. 1739 is utterly misdirected, however well intentioned it may appear to be. Those who own or control copyrights require no more money as an incentive for creativity. As for everyone else -- the "struggling" artist -- virtually nothing would ever trickle down.

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[18] Salmans, A Song Plugger's Biggest Play: His Return as Boss, N.Y. Times, June 4, 1985, at D1.

[19] According to the Recording Industry Association of America (the "RIAA"), music publishers achieved a tremendous 38% return on revenues in 1977, 39% in 1978, and 34% in 1979. Summary of Proposed Findings of Fact and Conclusions of Law, CRT Docket No. 80-2, at 4 (Nov. 17, 1980). See also infra, note 37 and accompanying text.

IV. The Contractual Rights of Artists

Given, then, that performers and songwriters generally do not hold copyrights in the songs that they record or write, they must rely upon contractual rights, as distinct from the operation of the copyright law, to be paid for their creative efforts. The heart of the recording industry's argument in support of S. 1739 is that the financial benefits of the royalty tax would flow through to the artists by contract. This claim, however, is contradicted by the facts about how contractual arrangements in the music business are structured.

Two types of contractual arrangements are used to compensate artists for the sale of prerecorded music. Performers -- recording artists -- contract directly with record companies. Songwriters rely on music publishers to negotiate contracts for the first recording of their compositions; thereafter, the mechanical royalty provisions of the copyright law[20] afford some minimal compensation -- through music publishers -- for subsequent recordings.

A. Negotiations Between Record Companies And Performers

Although a record company assumes the expenses of bringing an album to the market, its contracts with recording artists ensure that it is afforded maximum financial protection. Successful records will pay for themselves and provide the company with a handsome profit; record companies try to make certain that the costs of unsuccessful albums, however, will, to the fullest possible extent, be borne by recording artists.

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[20] 17 U.S.C. § 115.

Artists receive a small percentage of the profit on the sales of prerecorded music as a "royalty."[21] The costs of producing and promoting the record, designing the album jacket, and other record company expenses are, however, offset against the future earnings potential of the record. Typically, it is only when sales revenues exceed such expenses that a recording artist will see any money from his or her creative efforts.

If struggling artists, who, by definition, earn the least from the music business, are to benefit at all from S. 1739, it is only because the industry will reverse historic patterns and decide to act in an atypically philanthropic manner. Such artists will have to rely on the industry's benevolence because they have little, if any, bargaining power. They cannot insist on recording contracts that will pay them any more than what is standard within the industry, particularly when they negotiate with one of the six companies that collectively control more than 80% of the market.[22]

The industry's current practice, however, emphatically suggests that struggling artists will not benefit from S. 1739. Even moderately successful artists earn only a fraction of the revenues that a record company receives from the sales of a hit record.

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[21] In some cases, an artist -- particularly performers such as studio musicians -- simply will be paid a flat fee for a recording session.

[22] See supra note 7 and accompanying text. CBS distributes the Columbia, Epic, and the independent Chrysalis labels; RCA distributes the RCA-Victor, Arista, and the independent A&M labels; Warner distributes the Warner, Atlantic, and Elektra/Asylum labels; Polygram distributes the Mercury, Casablanca, Polydor, Capricorn, and RSO labels; Capitol distributes the EMI, Capitol, and Ariola labels; and MCA distributes the MCA, Coral, and the independent Motown labels.

Quite often an artist receives royalties on the basis of the suggested retail list price, minus some recording industry-imposed reductions. The royalty for sales within the United States is generally between five and ten percent of the suggested retail list price.[23] (Industry superstars, of course, are likely to receive somewhat larger royalties.) Royalties on foreign sales typically are much less -- only about one-half of those on U.S. sales.[24] These already small royalties are reduced even further by a series of record company costs, deductions, and offsets, which are briefly summarized as follows:

First, the price on which royalties are paid is reduced by approximately ten percent, to reflect the cost of packaging the record. The packaging deduction on tapes usually is higher, amounting to approximately fifteen percent of the suggested retail list price. The company reasons that the recording artist is entitled to royalties on the revenues generated from the recorded material, not on the value of the artwork and marketing material contained on the album package.[25] Thus, on an album that lists for $8.98, a record company might allocate $.90 to packaging, leaving the recording artist with a maximum royalty of five to ten percent of $8.08.[26] Thus, on this album, the performer would receive, at most, and before offsets and deductions, between $0.404 and $0.808 per record sold.

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[23] See, e.g., Shemel & Krasilovsky, supra note 6, at 4 (the royalty for a new artist may be as little as 4-1/2% to 5%, rising to 7-1/2% or 8% as the artist gains popularity). The royalty percentage on singles typically is lower than on albums, since the industry views singles as "loss leaders."

The discussion that follows is based upon a review of sample contracts of individual recording artists and of standard industry agreements.

[24] Id. at 5.

[25] Shemel & Krasilovsky, supra note 6, at 4.

Second, it has also been common industry practice to pay royalties on just 90% of total record sales. The ten percent reduction was intended to account for returns to the company of broken and otherwise damaged records.[27] As the incidence of breakage and imperfection has declined, this reduction has become less justifiable; it may still appear in a contract, depending upon the skills and knowledge of the person negotiating for the artist.

Third, approximately two percent of the albums sold will be labelled as "free goods," for which the record company will not pay royalties. These free records are claimed to be part of the cost of promoting an artist. (As many as three percent of singles may be considered "free.")

Fourth, record companies are likely to insist on reduced royalty payments for records that are distributed as part of a promotion or through a record club.

Fifth, and most significantly, payments to the recording artist are offset by many of the expenses incurred by the record company in producing and marketing the record. Usually, any payments are also reduced by any initial advances that the company has made to a performer.[28] (An "advance" is not a bonus payment, but merely a prepayment of expected future royalties.)

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[26] In certain circumstances, performers who are established may be able to increase this amount by negotiating for an escalation clause. Such a clause may entitle the artist to a higher royalty as total sales of a particular record increase.

[27] Shemel & Krasilovsky, supra note 6, at 4.

A recording artist, therefore, may not receive any royalties until all of the company's expenses and advances are recouped. Under this system, new artists, whose royalty percentages are low and whose royalty funds are small, may not receive any money for a lengthy period of time -- if ever -- after the release of an album.

The imbalance between parties to a recording contract is illustrated by the fact that a new artist might not receive any royalties on the sale of the first 100,000 albums, even though the record company might have collected gross revenues well in excess of $500,000 (assuming that the record company collects a standard percentage of the sales of an album with an $8.98 suggested retail list price). A seven percent royalty payable on 90% of the suggested price for 88% of the total record sales would entitle the artist to a maximum royalty of less than $50,000.[29] Furthermore, the record company is likely to claim that this amount should be offset against the costs of recording and marketing the album. The artist is left with no financial reward for making a reasonably successful record. In fact, the costs that the artist is obligated to repay under the terms of the contract are likely to exceed $50,000, meaning that the artist still would "owe" money to the record company. In short, the artist might not be entitled to any earnings from the sale of a substantial number of albums; the record company, by contrast, already might be making a significant profit.

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[28] Id. at 9.

[29] This assumes a ten percent reduction for broken albums, a two percent reduction for free albums, and no reduced royalty rate for premium or record club sales.

That this example is no mere hypothetical is illustrated by the career of Patty Smyth, an extremely successful, but still relatively new, recording artist. She has earned just $150,000 in two years from a retail gross in excess of $10 million. That is less than 1.5% of the gross earnings on her albums![30]

These contractual arrangements demonstrate the fallacy of the industry's argument: it is extraordinarily improbable that the record companies will allow recording artists to receive any monies from the royalty tax fund. To start, home taping royalties are not covered by current contracts, which pay performers on the basis of the suggested retail list price of a record. Moreover, except for successful performers, who have no need for additional financial incentives, such artists have little or no bargaining power vis-a-vis the recording companies. Even in the traditional core market for commercial exploitation of artists' works -- i.e., sales at the retail level, record companies make only the most begrudging payments.

Traditional industry recalcitrance makes it unlikely, therefore, that recording artists could ever succeed in convincing record companies to share the proceeds from a new revenue source -- the home taping levy. The more likely outcome is that the royalty tax fund will line corporate pockets and treasuries -- thereby doing nothing whatsoever to further the purposes of the copyright law.

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[30] Zaslow, New Rock Economics Make It Harder to Sing Your Way to Wealth, Wall Street Journal, May 21, 1985, at 1.

B. Compensation to Songwriters from Music Publishers: Mechanical Royalty Payments

As described above, songwriters are generally contractually dependent on the large publishing houses for receipt of royalties -- unless they are among the few successful singer/songwriters who can either form their own publishing companies or record their own compositions directly. Music publishers, like record companies, seek to structure such contracts in a way that will pay songwriters only a portion of the royalties that will be received from the exploitation of a song. And publishers, like record companies, also attempt to use at least some portion of the artist's royalty to recoup certain of the costs of marketing a song.

Owners of the copyright in a song are entitled to payment each time that a record or tape is made. For the first recording of a song, such payments are made pursuant to a contract between the record company and the entity owning the copyright in the song, i.e., usually the music publisher. Once a song is recorded, other performers and record companies can render their own arrangements of the song and record it, as long as the recording company pays (usually) the music publisher a so-called "mechanical" royalty for each copy that it makes of a record or tape containing said song.[31] Typically, songwriters' contracts with music publishers provide that something less than half of these mechanical royalties will be passed through to the composers or lyricists.[32]

The 1976 Act set the rate for mechanical royalties at 2-3/4 cents; the rate was adjusted upward to four cents by the Copyright Royalty Tribunal ("CRT"). Currently, then, at the rate of four cents per song, a songwriter will collect less than two cents from a record company each time his or her song is reproduced on a record or tape.

In cases where a songwriter is also a performer, and is negotiating directly with the record company for the first recording of the song, the company will often attempt to reduce the amount of the royalty that it must pay. In this situation, involving the initial recording, although the statutory mechanical royalty does not strictly apply, that royalty rate is generally considered the ceiling for payments to the artist. The record companies, however, have fiercely resisted the CRT's upward adjustment in the rate and so, in negotiations with artists, insist that it will pay only a percentage of the four cents per song. Only an artist with substantial market power may be able to collect the full four cents.

The amount that the songwriter receives from a record company via a publisher is reduced by the publisher to account for the cost of collection agency services. For mechanical royalties paid pursuant to foreign copyright laws for foreign pressings, the songwriter again only gets half of the fees paid to the publisher. These fees have also been reduced by deductions taken by the foreign companies involved in the production and collection process. Thus, the U.S. publisher might only receive some percentage, perhaps only half, of the mechanical royalties earned abroad. The songwriter, therefore, may only get one quarter of the foreign royalty to which he or she might legally be entitled.

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[31] See 17 U.S.C. § 115 (describing mechanical royalties).

[32] See generally Shemel & Krasilovsky, supra note 6, at 149-50.

Songwriters may get similar fractional portions of the royalties paid to publishers for the sale or reprint of sheet music and for "synchronization" fees, which are paid to publishers for the right to use music in television and motion picture soundtracks.[33]

As is true with record companies and recording artists, any advances paid to a songwriter generally are considered to be advance royalty payments. The publisher subsequently recoups advances out of the songwriter's share of royalties.[34] Promotional expenses may be borne by the songwriter either in whole or in part. In certain instances, publishers use the writer's royalty account to recover some portion of its expenses.[35] Thus, the cumulative impact of these contractual provisions is that, despite the 50-50 split of the typical songwriting agreement, a songwriter is likely to receive substantially less than half of all royalties paid to the music publisher.

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[33] The artist's share of any syncronization fee is calculated after deducting the licensing fee payable to an agency that typically is used to issue the synchronization license. See id. at 150.

[34] See, e.g., id. at 527-39 (AGAC Songwriter Contract Form, which contains the kinds of provisions discussed in the text).

[35] See id. at 150.

The practice of successful singer/songwriters -- of forming their own publishing companies to avoid such "trickle-down" payments -- demonstrates the restrictiveness of the constraints that music publishers place on an artist's potential earnings. This industry structure, in which the publisher (or an already wealthy singer/songwriter superstar) retains the majority of the royalties paid for the use of a song means that S. 1739 would only further enrich the rich.

The genuinely struggling composer or writer will see no money at all from the royalty tax fund. Those who are poor because their works are not being recorded will receive little compensation indeed from a levy that is to be distributed in accordance with the frequency of home taping. The bargaining clout of moderately successful songwriters, however, is so severely limited that even they will be unable to pry loose royalty tax monies from the music publishers who own the copyrights in their works.

IV. There Is No Reason To Expect That the Industry Suddenly Will Treat Artists Differently and Share Royalty Tax Funds with Performers and Songwriters

Past struggles between the recording industry and the creative artists show that most recording artists and songwriters will continue to receive only a small portion of the royalties earned in the music business. Struggling singers and songwriters are likely to see little, if any, of the money that consumers would be forced to pay.

Five years ago, when the CRT was considering an increase in the mechanical royalty, an argument was made that an expanded royalty pool, enhanced by record company payments, would benefit struggling songwriters. The argument was not unlike the one that the recording industry is now proffering in support S. 1739. At that time, the RIAA argued that any increase in royalties should not be based upon "the sympathetic imagery of the struggling songwriter."[36] The record companies recognized that the economic structure of the music business makes it virtually impossible for such artists to benefit from a change in royalty rates. It was clear then, as it is now, that no significant royalties flow to struggling artists. In the RIAA's own words:

> An increase in the [mechanical royalty rate] will inevitably result in enormous benefits for [established] singer/songwriters who are already richly rewarded for their creative efforts . . . . The struggling composer, on the other hand, will see little measurable benefit from an increase, and might actually suffer harm.[37]

Today, the industry suggests that added royalties would enable it to invest vast new sums of money in young artists or in new, innovative, or non-mass market music. That these promises are demonstrably hollow is made evident by the industry's failure to use its present enormous financial success to increase payments to new artists.

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[36] Prehearing Memorandum of the Recording Industry Association of America, CRT Docket No. 80-2, at 1 (filed May 5, 1980).

[37] Id. at 26-27.

To recapitulate briefly that success, the recording industry enjoyed two remarkable years in 1983 and 1984. In fact, 1984 was the industry's best year ever, with revenues of $4.5 billion.[38] Sales for the early part of 1985 have outpaced even the historic levels set in 1984.[39] Where are the industry announcements that it is signing or paying more to artists? Where are its plans to help finance the creative efforts of new singers and songwriters? To the contrary, there are indications that at least some record companies are moving away from such pro-creative initiatives by reducing the amounts they are willing to spend to develop "new" talent.[40] In the face of these facts, it is unseemly, at the least, for the recording industry to play on sympathies and emotions -- while seeking to extract hundreds of millions of dollars from the wallets of American consumer.

The industry is pretending that the proceeds from the royalty tax will assist struggling artists. Nothing in the legislation or in the industry's historical practices requires or suggests that there will be any earmarking of royalty taxes for new artists or specialized music. Indeed, there is nothing to prevent the industry from using home taping royalties for anything other than boosting shareholder dividends, lining the pockets of industry executives, or making acquisitions in other business areas. There is, however, no need for consumers to make further contributions to the industry's profitability. In sum, there is substantial evidence that the money collected in the royalty pool will not be used to stimulate creative endeavors and, therefore, that forcing consumers to pay a taping tax will not serve the purposes of copyright law.

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[38] See Horowitz, '84 a Peak Year for Recordings, Industry Net Shipments Worth $4.5 Billion, Billboard, Mar. 23, 1985, at 1.

[39] See, e.g., Grein, April Shower: Twice as Many Platinum Albums as '84, Billboard, May 11, 1985, at 11; Terry, U.S. Record Sales Still Upward Bound, Retailers Happy With 1st Quarter Results, Variety, Apr. 10, 1985, at 87.

[40] DiMauro, Disk Labels Play Cautions Game, Variety, Feb. 13, 1985, at 1 ("improvements in cash flow are not likely to precipitate sharp increases in artist signings at most labels").

V. Conclusion

The ultimate resting place of any revenues from a royalty tax is, then, entirely predictable. Such royalties will be used to advance precisely the same goals as those of present royalties: to recoup production and promotion expenses and to increase the profitability of record companies, music publishers, and industry superstars. The industry will continue to pay artists only a small fraction of the revenues received from the exploitation of songs and of sound recordings.

History belies the arguments of the recording industry. Such powerful companies never have been sympathetic to artists. It defies logic and economic reality to contend that they suddenly will rearrange industry structure to support the nation's performers and songwriters. Although emotionally appealing, the industry's argument should be unmasked and rejected for what it is: a clever ruse designed to force consumers to render tribute to the industry's already-overflowing corporate coffers.

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December 3, 1985

The Honorable Charles McC. Mathias, Jr.
Chairman
Subcommittee on Patents, Copyrights
and Trademarks
Committee on the Judiciary
United States Senate
137 Dirksen Senate Office Building
Washington, D. C. 20510

Dear Mr. Chairman:

At the October 30 Senate Subcommittee hearing on S. 1739, Senator Metzenbaum asked Mr. Gortikov some questions about the recording companies' recent profits and losses.[1] Mr. Gortikov's response seemed to suggest that profits are "down." In analyzing that assertion, we're all going to have to watch the numbers carefully -- there's some ledger-demain going on here.

The key to the numbers lies in just two facts:

1. 1984 was a great year for most record companies.

2. If 1985 profits are down (by no means are all companies in that situation), it's because 1985 is being compared to the great year of 1984. In other words, 1985 isn't bad -- it's just not as good as 1984.

That is the nature of a cyclical business -- a little bit up, a little bit down, sometimes a huge hit. One year Michael Jackson's Thriller album brings in record profits for a recording company. The next year, there is no substitute for the biggest selling album of all time, and the company shows a "reduction" in profits.[2] That's not a reason for a taping tax.

In short, "reduced" profits for a particular year or years do not provide a full picture of the recording industry's health. The fact that some recording companies are enjoying all-time record revenues in conjunction with lower profits may indicate simply that the companies are overspending or making unwise business decisions. In fact, after the recording industry's record-setting performance in 1978, music executives, convinced that good times were here to stay, invested in significant expansion. As recalled in a 1984 Washington Post article, record company spending was bloated by overstaffing, unrealistic contracts with some artists, and a general feeling that the boom times were going to last forever.[3] By his own admission, Walter Yetnikoff, now CBS President, stated that the problem was that CBS' "cost base was too high" and it "over estimated the size of the market."[4] The lost profits resulting from these poor business decisions aren't a reason for a taping tax.

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[1] Senator Metzenbaum also requested that I submit the articles, cited in the ARRC document "Taxing Blank Tape and Recorders: Untimely, Unnecessary, and Unfair," which substantiate our claim that the record industry is enjoying great success. I am enclosing those materials with this letter. Please include this letter and the accompanying enclosures in the hearing record.

[2] Washington Post, Nov. 24, 1985, at H1.

When considering profit data and the relative health of the recording industry, it is important to remind ourselves that six companies are in control of 85 percent of the market.[5] Thus, when the recording industry states that more than half of all recording companies are showing a loss, we have to keep in mind the relative market shares of the companies involved.

For example, for Warner Brothers, which controls 19 percent of the market, 1984 was its best sales year in its history, with almost 11 million copies of Prince's Purple Rain sold. Warner Brothers Records achieved all-time high revenues of $817.6 million.[6] Indeed, the figures for operating income and revenues provided in Warner Communications, Inc.'s ("WCI") 1984 annual report are even better than they appear because WCI shifted the allocation of home video revenues in its 1984 figures, so that home video profits are no longer included in the 1984 figures as they were in prior years.[7] Moreover, WCI's annual report indicates that the results for WEA International, WCI's overseas recorded music and home video distribution operation, decreased in 1984, which demonstrates that WCI's domestic increases in revenues are also more significant than the figures would otherwise show.[8]

WCI's operating profits for recorded music rose 42 percent in the first quarter of 1985 to $30.2 million from $21.3 million in the same period last year.[9] Operating profits for the nine-month period ending September 30, 1985 soared to $77,981,000 - an increase of 36 percent over the same period in 1984.[10] In sum, the company that accounts for one-fifth of the business is having a great year.

Another one of the big six, RCA, which represents 16 percent of the market, in 1984 also enjoyed a 4 percent increase in record sales to $621.8 million, primarily as a result of higher record club volume.[11]

RCA's Records and Video subsegment has continued its improvement in both sales and earnings in the first nine months of 1985. RCA states that these increases are due partly to the success of new domestic audio releases.[12] So that's another one-sixth of the industry doing extremely well.

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[3] Washington Post, Feb. 26, 1984, at G1.

[4] Id.

[5] Id.

[6] Warner Communications, Inc., 1984 Annual Report 1 (1984).

[7] Id. at 43.

[8] Id. at 18.

[9] Billboard, May 4, 1985, at 76.

[10] Variety, Oct. 23, 1985, at 77; Billboard, Nov. 2, 1985, at 6.

[11] RCA Corporation, 1984 Annual Report 31 (1984). RCA Records' profits in 1983 improved as a result of higher net volume and strong cost controls. Such improvements in profits as a result of a business decision to control costs underscores the fact that profit levels are tied as much to effective management as to sales volume.

[12] RCA Corporation, Quarterly Report for Quarter Ended June 30, 1985, at 9.

Similarly, MCA's Records and Music Group, which controls 8 percent of the market, had a terrific year in 1984, turning 1983's operating deficit of $7,974,000 into a 1984 profit of $8,839,000.[13] Revenues are continuing to increase in 1985 with revenues of $204 million for the first nine months, up from $179 million in 1984, and with operating income of almost $13.5 million, up from $5 million in 1984.[14] Adding WCI, RCA, and MCA together, that's 43% of the industry - nearly half - on a roll.

There are few figures available for Polygram, the American arm of a worldwide complex of record companies owned by Dutch electronics giant N.V. Philips, which controls about 9% of the market. But Polygram by its own admission has been profitable recently, with the worldwide group earning $30 million this year on consolidated sales of $75 million and Polygram contributing 10 percent of the profit.[15]

If you're counting, we're now over half the industry doing fine.

CBS Records, which occupies 24 percent of the market, produced the highest income in 1984 of any company in the history of the industry.[16] In 1984, CBS Records enjoyed profits of $123.5 million, which represented a 13 percent increase over 1983.[17] The fact that CBS Records has experienced a decline in profits in the first part of 1985 should be viewed in light of 1983 and 1984's banner profits and 1984's outstanding sales of Michael Jackson's *Thriller* album. Indeed, it is the new President of CBS, Al Teller, who is blaming CBS' decline in performance this year on the fact that the company's biggest acts have not been delivering albums by the dates for which they were targeted.[18] But while CBS may not have hit Michael Jackson levels this year, it's still solidly profitable.

So now we're up to 75% of the industry either *very* profitable or solidly profitable.

In sum, profit in the recording industry seems to be a function of the economy in general, artistic judgment, and the same kinds of cost controls and investment decisions that affect every other industry. In the face of the solid or excellent profits reported by the big 5, controlling 75% of sales, I'd like to see Senator Metzenbaum's question answered.

Sincerely,

Charles D. Ferris
Counsel to ARRC

cc: The Honorable Howard M. Metzenbaum

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[13] MCA, Inc., 1984 Annual Report 14 (1984).

[14] MCA, Inc., Quarterly Report for Quarter Ended June 30, 1985, at 3, 12; *Billboard*, Nov. 30, 1985, at 3.

[15] *New York Times*, Nov. 3, 1985, at 1F.

[16] CBS, 1984 Annual Report 3 (1984).

[17] *Billboard*, Feb. 23, 1985, at 4; CBS, 1984 CBS Annual Report 228 (1984).

[18] *Variety*, Oct. 9, 1985, at 117.

Taxing Blank Tape and Recorders: Untimely, Unnecessary, and Unfair

Audio Recording Rights Coalition
2001 Eye Street, N.W.
Washington, D.C. 20006
July 1985

Introduction

For almost 25 years, millions of American consumers have lawfully engaged in the practice of taping music in their own homes for their own personal enjoyment. Now, for the third time in four years, the U.S. recording industry has launched a major attack on that practice, and has asked Congress to levy a royalty tax on audio recorders and blank tapes. The Audio Recording Rights Coalition, representing consumer groups, audio tape and equipment manufacturers, retailers, and allied trade organizations, opposes the massive transfer of consumer dollars that this tax would entail.

The copyright property interest that the recording industry seeks to exploit is, as framed by the Constitution, a limited one. Authors and inventors receive protection only to the extent necessary to promote new works in the arts and sciences. Therefore, a proponent of more copyright revenue must look beyond desires for ever higher returns to the broader question of whether more money is now necessary to fulfill the public purposes imbedded in the Constitution. The recording industry has not even attempted to do this —perhaps because it is so clear that additional revenues cannot be justified. Instead, the reality that the recording industry must reconcile with its request for millions of consumer dollars is that the industry is today enjoying record-high revenues and profits, all generated by an avalanche of consumer spending on pre-recorded music. Copyright holders are thus obviously receiving more than enough money to stimulate creative output.

Whatever difficulties the industry may have experienced in the past were unrelated to home taping. Instead, the severe recession, video games and the billions of disposable dollars they gobbled up, and misguided industry practices were the culprits largely explaining the industry's condition in the early 1980's. The recession is now over, the video game phenomenon is dead, and the industry is finally operating more efficiently. Moreover, the industry is also finally (albeit belatedly) making prerecorded cassettes readily available at competitive prices. The payoff for the industry is unprecedented wealth.

The irony in the industry's attack on the home tapers is that these consumers are the industry's best customers. They buy more records than any other consumer group. More than half of the recordings they make are from records they have already bought and paid for. They tape to satisfy the demand for portable music that innovative recording products have created. And the very home taping practice the industry would now condemn often stimulates these consumers to purchase records after hearing those records on a home tape. This stimulative effect of home taping is more than enough reward for the industry, and the copyright law should not be used under the circumstances to further enrich the already wealthy.

I.

IN ORDER TO DEMONSTRATE THAT ROYALTIES ON AUDIO RECORDING EQUIPMENT AND BLANK TAPES ARE WARRANTED, THE RECORDING INDUSTRY SHOULD BE REQUIRED TO SHOW THAT MORE COPYRIGHT MONEY IS NEEDED TO PROMOTE MORE MUSIC CREATION AND DISSEMINATION

The conceptual framework in which the debate over home taping is taking place is established by the Constitution, which grants Congress the

> Power . . . to Promote the Progress of Science and Useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.

That framework has two elements, the first a goal and the second a means. The first element specifies the *purpose* of copyright: to promote the dissemination of scholarly and artistic works. The second element deals with rewarding creativity as a *means* to that end. The subordination of reward is obvious in the language of the Constitution, itself. That the Constitutional framework is still in balance was recently confirmed by the Supreme Court in *Sony Corp.* v. *Universal City Studios*, ____ U.S. ____ (1984).[1]

The Congress has expressly recognized that private gain of copyright holders is not, in and of itself, the proper purpose for establishing the scope of the copyright law.[2] From this framework, it follows that the proper test of whether consumers should pay additional copyright dollars is whether their dollars would promote the additional creation and dissemination of artistic works. The recording industry shirks that test, perhaps because the high level of artistic creativity and dissemination today—as measured by sales of recordings by new and established artists—makes it hard to argue that more money is needed to promote more musical creation. New technology, the would-be bogeyman, has in fact served both the public and the recording industry well. There has been no change in balance that needs to be redressed.

Instead of addressing the issue head on, therefore, the industry seeks to depict home tapers as pirates whenever they copy a recording for private, non-commercial use. Once home tapers are thus portrayed, it follows, in the industry's logic at least, that a royalty on taping equipment and blank tapes would merely recover revenue that was wrongfully taken.

This is not where the debate belongs. Consumers taping in their homes for personal and family use are clearly not wrong-doers, for the activity that the recording industry now seeks to condemn was expressly legitimized by Congress in 1971.[3] Equally important, the Constitution teaches us to focus not on copying as such, but rather on whether copying reduces creativity and should therefore be deterred by taxing it. Consumers should pay more only if it is clear that their doing so will lead to more artistic creation and dissemination. Otherwise, a new burden on consumers can only reduce dissemination, in contravention of the Constitutional copyright goal.

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[1] *See also United States* v. *Paramount Pictures*, 334 U.S. 131, 158 (1947) ("The copyright law . . . makes reward to the owner a secondary consideration.").

[2] *See*, for example, the House Judiciary Committee's report accompanying the Copyright Act of 1909, which noted that

> [t]he enactment of copyright legislation by Congress under the terms of the Constitution is not based on any natural right that that author has in his rights, . . . but upon the ground that the welfare of the public will be served and progress of science and useful arts will be promoted by securing to authors for limited periods the exclusive rights to their writings.

H.R. Rep. No. 2222, 60th Cong., 2d Sess. 7 (1909).

A second means by which the industry seeks to avoid the proper Constitutional test has been to issue dire forecasts about the imminent demise of the entire industry if consumers were allowed to continue untaxed audio taping in the privacy of their own homes.[4] These forecasts have been proved wrong on every score, and the unprecedented profitability of the recording industry today should silence once and for all those who guessed that home tapers would destroy the industry. Moreover, the profitability of the industry proves that the premises underlying the industry's assault on home taping are wrong. Before Congress seriously considers transferring millions of dollars from consumer's pockets to those of the recording industry, Congress should look very closely at recording industry claims then and now in light of the industry's actual experience and it should insist that the industry demonstrate how more consumer money could possibly be necessary to promote creation and dissemination of artistic works. This is a burden of proof which the recording industry must, but can not, meet.

II. HOME TAPING HAS NOT DEPRIVED THE RECORDING INDUSTRY OF NEEDED REVENUE

A. The Recording Industry Is Having Its Best Years Ever

In 1982 and 1983, the recording industry warned Congress that the continued free home taping of musical recordings threatened the industry's very existence. A rhetorical web was woven in which the non-commercial activities of consumers in their own homes would soon bring the industry to its knees if Congress did not take action against the home taping phenomenon. Congress did not act, and today, rather than gasping for its last breath, the recording industry is enjoying spectacular financial

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[3] In the legislative history accompanying the Sound Recording Amendment of 1971, Congress made clear its intent to exclude home taping from the reach of the copyright law:

> Specifically, it is not the intention of the Committee to restrain the home recording, from broadcasts or from tapes or records, of recorded performances, where the home recording is for private use and with no purpose of reproducing or otherwise capitalizing commercially on it. This practice is common and unrestrained today, and the record producers and performers would be in no different position from that of owners of copyright in recorded musical compositions over the past 20 years.

H.R. Rep. No. 487, 92d Cong., 1st Sess. at 7, reprinted in [1971] U.S. Code Cong. & Admin. News at 1572.

[4] *See* Recording Industry Association of America, Inc. "Audio Home Taping" at 7, *reprinted in Copyright Infringements: Hearings on S.1758 Before the Senate Comm. on the Judiciary*, 97th Cong., 1st & 2d Sess. [hereinafter *"Hearing on S. 1758"*] at 701; Statement of Stanley Gortikov at 1, *reprinted in Hearings on S.1758* at 711.

results. 1983 was the industry's best year since 1980, with total dollar revenues on prerecorded music sales of $3.81 billion. 1983 was then followed by 1984, which was the industry's best year ever, with revenues of almost $4.5 billion,[5] surpassing the previous $4.13 billion 1978 record level. The industry's success is not limited to a lucky few: every major record company enjoyed increased profits and revenues.[6] For example:

- **CBS Records Group led the way with an enormous $109 million operating profit on $1.15 billion of sales in 1983 and an all-time single company industry-high $123 million operating profit on $1.27 billion of sales in 1984.[7]**
- **RCA reported in its 1983 Annual Report that "[s]ales of audio records and cassettes increased and, combined with strong cost controls, resulted in significantly improved profits." That trend continued in 1984, with the Consumer Electronics Division boasting "record profits" through the third quarter.[8]**
- **WCI Record Group, including the Warner, Elektra/Asylum, and Atlantic labels, also called 1984 the "biggest year ever."[9] In 1985, WCI Record Group posted its highest first quarter revenues ever.**
- **Revenues from MCA's Record & Music Group (which includes some domestic home video sales) jumped to $255 million in 1984 from the 1983 total of $188 million.[10]**

As sales through early 1985 outpace even 1984's record-high rate, it appears that the 1983-84 recovery is here to stay.[11] Indeed, confidence is such that the industry is likening its success to the glory days of the 1960's and 1970's,[12] and, at least when they are not talking to Congress, industry executives are predicting that the climb will continue.[13] Retailers obviously agree, as demonstrated by a wave of new investments.[14]

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[5] *See* I. Horowitz, "'84 A Peak Year For Recordings, Industry Net Shipments Worth $4.5 Billion," *Billboard*, Mar. 23, 1985 at 1; *see also* K. Terry, "Record Biz Makes A Strong Comeback, Buyers Respond To New Music," *Variety*, Jan. 26, 1985 at 195.

[6] Remarkably, the industry is enjoying these results even while many of its most avid customers are waiting for it to supply adequate quantities of compact discs—the industry's hottest new item. When enough of these are available, customers will make purchases they have been postponing, and many will re-create their entire collections. Thus yet another "hardware" invention will turn out to be a bonanza for a "software" industry.

[7] "A Year for Records," *Fortune*, Apr. 1, 1985 at 10; 1983 *CBS Annual Report* at 47.

[8] "RCA Reports Hike in Earnings," *Billboard*, Nov. 10, 1984.

[9] S. Sutherland, "Warner Bros. Music: 'Biggest Year Ever,'" *Billboard*, Mar. 16, 1985 at 6.

[10] "Music Brightens Picture For MCA Inc.," *Billboard*, Mar. 2, 1985 at 86.

[11] K. Terry, "U.S. Record Sales Still Upward Bound, Retailers Happy with 1st Quarter Results," *Variety*, Apr. 10, 1985 at 87. P. Grein, "April Shower: Twice as Many Platinum Albums as '84," *Billboard*, May 11, 1985 at 1; "RIAA Metal Awards Show Increase in March," *Variety*, Apr. 10, 1985 at 87; E. Paige and F. Goodman, "Feb. Sales Have Strong Heartbeat," *Billboard*, Mar. 2, 1985 at 22.

[12] M. Potts, "Studios Grooving to Pop-Music Revolution," *Washington Post*, Feb. 26, 1984, at Gl.

[13] *Id.*

[14] *See* J. Sippel, "Chains See Ambitious Expansion," *Billboard*, Sept. 15, 1984 at 3 (quoting Robert D. Summer, President of RCA Records, saying "[t]here's some real good hard reasons to believe that the industry now has enough power to continue its climb").

Had the industry's past predictions been well-founded, none of the industry's recent success could have occurred as long as home taping continued unabated. Home taping did continue, however, and thus other factors must have accounted for the industry's doldrums in 1982. One obvious cause, as we said at the time, was the severe 1982 recession; with the overall economic recovery the recording industry recovered as well. Another problem in 1982 was the diversion of billions of dollars into Pac-Man and other video games in both the arcade and the home; when this phenomenon ran out of steam, billions of consumer dollars were freed up to return to the music industry.[15] Other important reasons, which warrant the separate discussions to follow, include the industry's success in signing and promoting the stars of the 1980's; the industry's recent (but belated) adaptation to the new market in which consumers seek music in portable form; and the industry's recent (but belated) adoption of prudent business practices.[16]

In its best light, the industry's grab for more copyright money reflects a misunderstanding of its own history and of what home taping represents. In another light, the grab reflects simple, unrestrained greed. But whatever the industry's motive, the size and strength of the industry's recovery has shown that home taping is not the doomsday device for record sales and music production that the industry would have Congress believe. Moreover, the success of the entire industry demonstrates that royalties on tapes and taping equipment are not required to stimulate creative achievement, since copyright holders are now receiving more money than ever before.[17]

B. Much Of The Industry's Success Is Attributable To Its Belated Adoption Of Changes Required By The Market

1. The Industry Signed The Stars And Is Reaping Fabulous Results

As recently as two years ago the recording industry was bemoaning the loss of the top end of the market and blaming home taping for the absence of spectacular stars.[18] We said then that this was a lame excuse for the industry's failure to find and sign the artists that the music-buying public wants to hear, and events have borne us out. In the last two years—while sales of audio taping equipment continued to expand—the industry has experienced fabulous sales of records by the superstars of the 1980's.

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[15] Gross collections from coin operated amusements (video games and jukeboxes) fell from $8.9 billion in 1982 to $4.5 billion in 1984. "Play Meter Magazine Annual Operators' Survey," Nov.1, 1984 at 32. In addition, average weekly gross collections for video game machines fell from $140 dollars per machine in 1981 to $53 dollars per machine in 1984. *Id.* at 35.

[16] Some other reasons cited by retailer Bill Golden in a bullish state-of-the-industry report to the National Association of Record Merchants Advisory Committee include successful promotion tours, hot sound tracks, return to record buying by older customers, and absence of major price increases. E. Paige and A. White, "NARM Advisory Committees in Wide-Ranging, Constructive Meeting," *Billboard*, Oct. 6, 1984 at 22. *See also* S. Sutherland, "Wall Street Bullish on Music," *Billboard*, Nov. 24, 1984 at 1.

[17] We are not saying that, because of home taping, the recording industry is guaranteed permanent commercial success. Its success has tended to be cyclical. Events have supported our argument, however, that home taping did not cause the slump in 1982 and, if anything, has sparked the present boom.

[18] *See* K. Terry, "Home Taping Blamed For Part of WCI Group Slump, Top Earning LP's Most Affected," *Variety*, Feb. 23, 1983 (interview with Elliott Goldman, Senior Vice President at WCI, following the issuance of a Warner report blaming home taping, in large part, for WCI's 1982 slump in sales).

The greatest mega-million album during the last two years has been the Michael Jackson "Thriller" album. 37 million copies have been sold worldwide (20 million in the United States), making "Thriller" the most popular album of all time.[19] Other albums have also sold fabulously well, and a crowded field now finds itself at the top end of the market that the record industry said was forever lost to home taping. Prince sold 9 million "Purple Rain" albums,[20] Lionel Ritchie sold 8 million "Can't Slow Down" albums, Bruce Springsteen became Columbia Record's all-time best seller with U.S. sales of 6.5 million copies of "Born in the U.S.A.,"[21] Huey Lewis and the News sold 5 million "Sports" albums, and Van Halen sold 5 million "Jump" albums.[22] The recently released Chicago 17 album is the band's biggest album ever, with 4 million copies sold.[23] Four million copies of the "We Are The World" single were shipped within six weeks of its release, and two million albums were sold in less than six weeks.[24] In addition, platinum and gold album certifications rose sharply in 1984[25] and again in 1985,[26] and one keen industry observer, Howard Turetsky of Lehman Brothers, has been quoted as saying that "the mega-album has come back."[27]

The proliferation of the mega-albums conclusively rebuts any claim that home taping has taken away the top end of the market. Moreover, as the industry draws up to the Congressional well a third time, it must now contend with the fact that the success of its major artists has invalidated its argument that home taping had forever robbed it of the chance to make extraordinary profits on sales of the blockbuster album. Instead, the industry must explain how home taping can be harmful if the albums most likely to be taped are enjoying unprecedented success.

2. The Industry Is Finally Exploiting The Market For Portable Music

Experience has proved that we were right in the past when we said that the recording industry's failure to adapt to the market was a far more important cause of loss than any sales lost to home taping. Today, the industry is reaping rewards for its belated marketing of prerecorded music in portable, cassette form. They are finally seizing the benefits that new technology offers them.

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[19] *1983 CBS Annual Report* at cover page; K. Terry, "Record Biz Makes A Strong Comeback," *Variety*, Jan. 26, 1985. Seven of *Thriller's* nine songs were released as singles, and each song received significant airplay and attained "gold" status.

[20] The 9 million copies of "Purple Rain" sold in 1984 established a single year's high for domestic sales of an album. "Inside Track," Billboard, Feb. 23, 1985 at 74.

[21] "Longplay Shorts," *Variety*, May 1, 1985 at 492.

[22] "Top Pop Albums," *Billboard*, May 11, 1985 at 74; "WCI Music Profits 'Jump'—Van Halen Album Cited," *Billboard*, May 5,1984 at 4.

[23] *Billboard*, Mar. 2, 1985 at back cover.

[24] S. Dupler, "'World' Album Off To Fast Start," *Billboard*, April 13, 1985 at 3; "Top Pop Albums," *Billboard*, May 11,1985 at 74.

[25] P. Grein, "Big Jumps In Platinum, Gold, RIAA '84 Totals," *Billboard*, Jan. 12, 1985 at 1.

[26] P. Grein, "April Shower, Twice as Many Platinum Albums as '84," *Billboard*, May 11, 1985 at 1.

[27] K. Terry, "Record Biz Makes A Strong Comeback, Buyers Respond To New Music," *Variety*, Jan. 26, 1985 at 196; D. Wishik, "Registers Ringing At Record Shops," *USA Today*, March 5, 1984 at B2.

When the industry first asked Congress to impose a royalty tax on audio taping equipment and blank tapes, it claimed that massive sales of records were being lost to tapes made by home tapers. To that claim we answered that cassettes were proliferating not as substitutes for hard vinyl disks, but because U.S. consumers increasingly wanted recorded music in portable cassette form. We were right. While disk sales have consistently declined over the last four years (204.6 million units in 1984, down from 295.2 million units in 1981), prerecorded cassette sales have soared to 332.0 million units in 1984, an increase of almost 200 million units from the 137.0 million units sold in 1981.[28] In 1984, sales of prerecorded cassettes accounted for a dollar volume of $2.38 billion, over 55 percent of the industry's total revenues, and account for the recording industry's revival.[29] The move to cassettes is consistent with survey evidence that more than half of all recordings of copyrighted music made at home for personal use are from records the user *already owns.*[30]

The industry held off prosperity by failing to understand the portable music revolution inaugurated by introduction in 1980 of "Walkman" and other high-fidelity portable cassette players. Instead of adapting to the new consumer demand, the industry threw substantial resources and energy into battling the very home taping phenomenon that the industry's inattention fueled. Had the industry devoted comparable resources to market adaptation, its spectacular recovery might well have begun earlier. But the record industry was like a sleeping giant, convinced of the costs of new technology but with its eyes closed to the benefits.

Consumers seeking music for their Walkman and for their car stereos were forced to turn to their home taping equipment to satisfy their demand for portable audio material, since the selection of prerecorded tapes was so limited.[31] Since 80 percent of all home tapers also owned one or more portable tape players, the amount of home taping done to meet this need was substantial.[32]

Now that the recording industry has taken its head out of the sand and is producing large quantities of prerecorded cassettes for play in car stereos and Walkman-type devices, it is perhaps beginning to realize that home tapers may be responsible for the industry's bonanza. As Russ Solomon, President of Tower Records, said in a recent interview:

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[28] "Manufacturers' Unit Shipments," RIAA press release dated Apr. 1, 1985.

[29] "Disk Industry Up 15% For '84; Cassettes Are The Key," *Variety*, Apr. 10, 1985 at 87; "RIAA Figures: Cassettes Paced A Record '84," *Billboard*, Apr. 13, 1985 at 1; P. DiMauro, "Orders Hold Up At Pressing Plants," *Variety*, May 1, 1985.

[30] Yankelovich, Skelly and White, Inc., "Why Americans Tape: A Survey of Home Taping in the United States," July, 1982 ["Yankelovich Survey"] at 54.

[31] The Yankelovich Survey conducted in 1982 detected this, finding that fully 75 percent of tapers cited portability, and 57 percent cited convenience, as "very important" reasons for sometimes using home-recorded tapes instead of records. Yankelovich Survey at 18, 69-76. Over a quarter of those who taped albums most often did so to make copies of records for listening in their cars or offices. Warner Communications, Inc., "A Consumer Survey: Home Taping," March 1982 ["Warner Survey"] at 16.

[32] A third of the tapers in the Yankelovich Survey complained of limited tape availability (32%), and almost a quarter (21%) reported that music stores' stocking and selling practices made it difficult for them to buy those tapes that did exist. Yankelovich Survey at 89-90. Seven percent (7%) of tapers in the Warner Survey gave the unavailability of prerecorded tapes as the single reason they most often made a home music tape. Warner Survey at 17.

> [I]f you didn't have the home-recording business, you wouldn't have Walkman machines. In other words, the tape technology that came out of the recording machine resulted in the portable playback machine and the automobile machine, which created an enormous market for us.[33]

In short, it is far from a coincidence that recording industry fortunes have improved at the very time home taping equipment proliferated.

Although the industry is finally benefitting from better satisfying consumers' demands for portability, significant further gains could be achieved if the industry improved the quality of its prerecorded cassettes. The industry's cassette tapes generally use inferior material and shells, causing inexact tracking during play, and are duplicated at speeds—64 times normal play speed—that cause inferior playback quality.[34] Many consumers are not satisfied at that low quality level, and, to achieve the audio quality they seek, they make their own much higher fidelity recordings by selecting high quality material and shells and by duplicating at normal play time. The record industry is now only starting to actively explore high quality prerecorded cassettes. If the industry seeks still more revenues than it achieved in record-breaking 1984, then it should complete its adaptation to today's market, which home tapers have largely shaped.

3. The Industry Has Begun To Operate Efficiently

The recording industry has also begun to cut costs and drop those activities that drained away its profits. CBS showed one way to cut costs when, in 1982, it closed two factories and half of its branch sales offices under the pressure of recession and increased competition.[35] Another way the industry reduced costs was to tighten inventory controls.

The most important cost-saving measure by far, however, was the industry-wide decision to stop signing contracts with a large number of artists and performers on a hit or miss basis in the hope that a successful artist might emerge. The industry's recession forced it to focus its resources on fewer artists who offered reasonable prospects for success and, not surprisingly, these more selective signing practices have led to significantly improved returns.[36] New technologies have altered the nature of the market by making previously unattainable exposure (the 17.5 million subscribers to MTV) available to a few, heavily- backed artists.[37] Now that the industry has had several years experience with efficient operations using fewer artists, it is inconceivable that it would revert back to its less efficient and less profitable approach, even if more copyright dollars were made available.

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[33] M. Goldberg, "The Wisdom of Solomon," *Rolling Stone*, Nov. 22, 1984 at 39.

[34] *See generally* Testimony of Edward J. Foster, President, Diversified Science Laboratories before the Senate Judiciary Committee, October 25, 1983 at 9 *reprinted in Video and Audio Home Taping: Hearings on S.31 and S.175 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary*, 98th Cong., 1st Sess. 443. Mr. Foster also pointed out that prerecorded cassettes are issued on the *lowest* grade of audio tape available, which, he said, belies the notion that the market for blank tape can be segmented according to use.

[35] *See* S. Salmans, "The King of CBS Records," *N.Y. Times*, Jan. 22, 1984 at F7 (quoting Walter Yetnikoff, President of CBS Records, boasting that CBS "did cost-cutting that would make Chrysler proud.").

[36] P. DiMauro, "Disc Labels Play Cautious Game, Once Burned, Twice Shy On Signing," *Variety*, Feb. 13, 1985 at 1.

C. The Recording Industry Misunderstands The Nature Of Home Taping And Grossly Inflates Its Minimal Impact On Sales Of Prerecorded Music

The relationship between home taping and prerecorded music sales has been much analyzed, but the fundamental question of "who tapes what and why" has consistently eluded definitive quantification. What is clear, though, is that the recording industry is wrong in arguing that home taping has a destructive effect on music sales and in flatly denying taping's positive effects on the music industry. Instead, home taping complements prerecorded music sales, both because it stimulates record sales[38] and because, in the earlier years, home taping developed the ready market for the prerecorded cassettes that are fueling the industry's revival. So much so, in fact, that it is appropriate to ask whether home taping's stimulation of the industry's revival is not reward enough for the recording industry.

1. The Home Taper Is The Industry's Best Customer

The irony in the industry's assault on home taping is that the industry's own surveys agree that the typical home taper is the industry's best customer. Thus, the Roper Survey stated:

> Based on reports from all adults, those who record music on tape are much heavier buyers for their own use of records, pre-recorded tapes and blank tapes than are nonrecorders . . .
>
> Roughly twice as many adult tape recorders as nonrecorders buy LP records, singles and pre-recorded 8-track tapes. Four times as many recorders as non-recorders buy prerecorded cassettes . . .[39]

A 1979 survey by Scali, McCabe, Sloves, Inc., showed that purchasers of a name brand blank tape averaged over 11 phonographic record purchases in 1979. The Warner

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[37] G. Fabrikant, "The Record Business is Solid Gold Again," *Business Week*, Feb. 15, 1985 at 35 (quoting CBS's Yetnikoff, "You can no longer just throw a record out there and hope it will stick."); J. Zaslow, "New Rock Economics Make It Harder To Sing Your Way To Wealth," *Wall Street Journal*, May 21, 1985 at 1.

[38] The Yankelovich Survey found, for example, that consumers often buy an album after taping all or part of it. Yankelovich Survey at 16, 45-48. In addition, consumers often discover a performer by listening to a home tape, then purchase other works by that performer. *Id.*

[39] Roper Organization, Inc., "A Study on Tape Recording Practices Among the General Public" (1979) ["Roper Survey"] (Conducted for the National Music Publishers Association and the Recording Industry Association of America; unpaginated). Eight out of ten (82%) of the tapers surveyed were current buyers of records and prerecorded tapes, while only 44% of non-tapers reported purchasing prerecorded music. Warner Survey at 32. According to the CBS Survey, 80 percent of blank tape buyers also purchase prerecorded music. CBS Records Market Research, "Blank Tape Buyers: Their Attitudes and Impact on Pre-recorded Music Sales" (1980) ["CBS Survey"] at 6.

Survey explained this phenomenon by noting that

> [b]uying and taping both reflect a more general commitment to music. That is, the more one sees music as important, the more likely one is to engage in both buying and taping.[40]

Perhaps *Rolling Stone* magazine summed up best the irony of the industry's assault on home tapers when it said that

> [h]ome tapers aren't a bunch of freeloaders, they're the very people the record industry depends on to turn a release platinum .... In essence, the record industry is saying that its best customers are its worst enemies.[41]

Thus, a home taping royalty would force the consumers already paying the most copyright dollars to pay even more.

2. The Recording Industry Ignores The Huge Amount Of Taping That Does Not Involve The Reproduction Of Its Products

The recording industry would have Congress believe that, with few exceptions, taping involves the reproduction on tape of the identical product that the industry sells. That view of taping is grossly mistaken. Indeed, even where records are the source of tapes, much of home taping is done for the purpose of creating customized anthologies, either for personal libraries or party entertainment use.[42] Obviously, this type of taping activity does not displace record sales. If anything, selective home taping stimulates record sales and is thus a source of more, rather than less, copyright money.[43]

Another aspect that the industry glosses over is that a lot of taping activity does not involve the taping of copyrighted music. Tapers use audio tape for a myriad of reasons, including family, educational,[44] and business purposes. In the home, more than half of all home audio taping is done for some purpose other than taping prerecorded music.[45] For example, the Yankelovich survey found that almost half of all home tapers tape music performed by themselves or their family or friends, such as a child's musical recital or an amateur rock band.[46] Audio taping is also a common element of traditional festivities, such as weddings and birthday parties.[47] Indeed, a quarter of all home tapers never even tape prerecorded music,[48] with telephone answering machines and the taping of personal correspondence accounting for a large amount of non-copyright-related uses. Outside the home, businesses, the government, and others make extensive purchases of audio tape machines and blank audio tapes for taping material other than copyrighted pre-recorded music. Some of these non-copyright uses include:

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[40] Warner Survey at 36. Those who both tape and buy prerecorded music are more likely than others to rate themselves as knowledgeable sources of information about prerecorded music (38% affirmative for tape-buyers compared to 20% for tapers-only/18% for buyers-only), and are more likely to consider themselves "collectors of prerecorded music" (51% versus 17%) and to discuss prerecorded music with others (38% versus 6% of non-tapers). Warner Survey at 37-38. Tapers are also substantially more likely than non-tapers to go to live concerts (55% compared to 30%), to read about music (62% versus 36%), and to prefer receiving records and tapes to other items as gifts (74% versus 40%). Warner Survey at 39.

[41] "The War Against Home Taping," *Rolling Stone*, Sept. 16, 1982, at 59, 64. Now that the industry is marketing portable cassettes, this is becoming even more true, as more and more home tapers are buying the industry's prerecorded cassettes to save themselves the time and energy involved in making their own. *See* M. Goldberg, "The Wisdom of Solomon," *Rolling Stone*, Nov. 22, 1984 at 39 (quoting Russ Solomon, President of Tower Records, saying that "[a] lot of people find it inconvenient and time-consuming to tape on a regular basis, so they end up taking the easy way out. They buy the tape. That's what seems to be happening. We're not selling a blank tape at the expense of selling a record.").

[42] According to the Warner Survey, respondents spent over half (56%) of their taping time making recordings of selections. Warner Survey at 15.

[43] *See* M. Goldberg, "The Wisdom of Solomon," *Rolling Stone*, Nov. 22, 1984 at 39 (quoting Russ Solomon calling blank taping "the Hamburger Helper of the music business. The record that you are taping is a record you very well may have bought. You tape a copy for your car."). Indeed, surveys show this to be the case more than half the time. See note 33, *supra*.

[44] Forty-five percent (45%) of home tapers use audio tape for educational purposes, such as taping lectures. Yankelovich Survey at 14, 36.

- *Office dictation*—According to the Computer and Business Equipment Manufacturers Association Marketing Data Book, approximately 550,000 dictation machines are sold annually in the U.S., suggesting that millions of machines are in existence, using even more millions of blank tapes.
- *Private reporting services*—Private reporting services necessarily account for a vast amount of the blank tape consumed in America. The National Shorthand Reporter Association has 18,000 members; assuming an equal number of reporters using taping devices (a low cost way of transcribing proceedings), they would account for 36 million hours of taping per year (at forty hours per week per person). Again, millions of blank tapes are consumed for the taping of non-copyrighted materials.
- *Educational institutions*—Colleges and universities represent a vast consumer of blank tapes for non-copyright use. Not only do professors use tapes as a means to teach foreign language skills, but students use tapes to record lectures and study sessions. An informal canvassing of various foreign language departments has shown that each purchases several thousand tapes for their language labs alone. The 85,000 public schools and secondary schools in the U.S. also use blank tapes for non-copyright related uses.

Although exact numbers are impossible to come by, it is clear that tens of millions of blank tapes are used by consumers and institutional users in ways that do not even encounter copyrighted works. Taxing these uses would be a windfall for the record conglomerates, unfair to consumers, and overbroad.

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[45] Specifically, "home tapers" (persons who made a home audio recording of any kind in the last two years) recorded something other than prerecorded music on 52% of the tapes they made in the three months preceding the Yankelovich Survey. Yankelovich Survey at 14, 35. In other words, fewer than half of the total tapes recorded at home contain prerecorded music.

[46] Yankelovich Survey at 14, 37-38.

[47] *Id.* More than eight out of ten home tapers (82%) have used audio tapes to record something other than prerecorded music. Yankelovich Survey at 35.

[48] Yankelovich Survey at 15, 29. As well, 44% of tapers age 50 and over have *never* taped any prerecorded music. Yankelovich Survey at 15, 42-43. A study commissioned by the Copyright Royalty Tribunal confirmed that over half of home tapers (57%) do not tape music at all. *See* Wm. R. Hamilton, "A Survey of Households with Tape Playback Equipment," at 5 (Sept. 1979).

III. EVEN IF A HOME TAPING ROYALTY WERE IMPOSED, THE MUSICIANS WHO MIGHT BE STIMULATED TO GREATER CREATION WOULD RECEIVE VERY LITTLE OF THE MONEY

Because of the way the music industry operates, most copyright money flows into the pockets of the industry's established powers—the record companies, music publishing companies, and a handful of wealthy superstars. Hence, a home taping royalty would not further the Constitutional goal of promoting additional musical creation and performance, since those most responsive to increased compensation—struggling singers, musicians, and songwriters—might get nothing, and, at most, would receive only a tiny portion of the royalty.

When a recording company sells a record, the singers and instrumentalists don't necessarily get a share of the purchase price. Performers often work for a flat fee, paid by the record company, in exchange for signing away their rights in the "sound recording." So even if the record is a huge hit, they get no more than their "session fees"; the record company gets all the royalties from the performers' work.

Other performers sign away their rights in the sound recording in exchange for a share of the record revenues, as agreed on by contract between the performer and the record company. The problem is that the unestablished performer in these negotiations is likely to confront, on the other side of the table, one of the six record companies—WCI,[49] CBS,[50] RCA,[51] MCA,[52] EMI-America,[53] and Polygram[54]—that dominate the recording industry. Each of these companies is huge in its own right,[55] and not surprisingly, the negotiations between performers and these companies usually take place on highly uneven terms; inevitably, few performers get much of the profit on the records they create. A stark example of this phenomenon was laid out in detail in a recent front-page *Wall Street Journal* article, which described how one of today's biggest new stars—Patty Smyth—earned less than $150,000 out of a total retail gross exceeding $10 million dollars over a two year period.[56] For the lesser performer—the struggling artist—the payout is likely to be a mere token.

Unestablished composers are in no better position than workaday musicians. The composer can either attempt to market his songs to performers himself or turn his work over to music publishing companies in hopes that the music publisher will persuade a performer to record the song and—with luck—create a hit. The publishers exact a huge price for their effort—a full 50% of *all* the composer's royalties for the song—whether or not the publisher actually had a hand in getting it recorded.

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[49] Warner Brothers, Atlantic, and Elektra/Asylum labels.

[50] Columbia, Epic, and other labels.

[51] RCA-Victor and Arista labels.

[52] MCA and Coral labels.

[53] EMI, Capitol, and Ariola labels.

[54] Polydor, RSO, Casablanca, and Capricorn labels.

[55] The industry is a classic oligopoly with six major conglomerates controlling virtually the entire market. In 1984, the Federal Trade Commission moved to block the proposed merger of number two WCI with number six Polygram due to fears that the resultant super-conglomerate would mean less competition and higher prices. As a result of the FTC's challenge of the proposed merger, WCI and Polygram dropped their merger plans.

[56] J. Zaslow, "New Rock Economics Make It Harder To Sing Your Way To Wealth," *Wall Street Journal*, May 21, 1985 at 1.

Consider one common sequence, for example. A composer assigns a song, and 50% of his royalty rights, to a music publishing company which makes it available to a singer, who records it. As the song starts to get airplay, other musicians hear it on the radio—not from the music publisher—and decide to record it. Under current copyright law, any performer can record any song that has been previously recorded, without either the composer's or publisher's permission, by paying a compulsory royalty. And every time any performer records a song, the music publisher who introduced it to the first performer gets half the royalty, even though it had literally nothing to do with fostering any recordings after the first one. Some people would call that "a license to print money."[57] Indeed, business is so good for the publishing houses that the owner of a New York music publishing company, Chappell & Co., recently confessed to the *New York Times* that "[Y]ou can't lose money" and "[I]t's the most unbelievable business."[58]

Interestingly, the recording companies, which when they seek royalty taxes tell Congress about the need to reward struggling songwriters, tell a very different story when they have to split the pie with composers. In 1980, RIAA told the Copyright Royalty Tribunal that an increase in copyright income for composers should not be based upon "the sympathetic imagery of the struggling songwriter."[59] The RIAA could almost have been speaking for ARRC:

> An increase in the [musical works royalty] rate will inevitably result in enormous benefits for [established] singer/songwriters who are already richly rewarded for their creative efforts. . . . The struggling composer, on the other hand, will see little measurable benefit from an increase, and might actually suffer harm.[60]

Given the interposition of the record companies and the publishing companies between the copyright dollar and the singer/songwriter, it is no surprise that the only musicians to benefit significantly from their music are the handful of superstars who possess sufficient market power to exact favorable contracts from music publishing and record companies, or set up their own. These musicians, however, are among those least likely to be induced to new musical creation by more money. How much more inducement beyond the $70 million he received from his "Thriller" album does Michael Jackson need to create more music?

In view of the way the copyright system actually operates, Congress should be extremely wary of claims that a proposed home taping royalty will benefit struggling artists. The only home taping tax revenues most performers would actually see are those which the record company gives them by contract, and no bill is going to change the industry's penchant for squeezing a record for virtually all it's worth, leaving only a trickle of money for performers. As for songwriters, they come second behind the music publishers, whose half of all new royalty taxes, up front, will do nothing to entice composers to compose.

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[57] Music publishers are very prosperous, much more so than composers. According to the RIAA, they achieved a tremendous 38% return on revenues in 1977, 39% in 1978, and 34% in 1979. "Summary of Proposed Findings of Fact and Conclusions of Law," CRT Docket No. 80-2, Nov. 17, 1980 at 4.

[58] S. Salmans, "A Song Plugger's Biggest Play: His Return as Boss," *New York Times*, June 4, 1985 at D1.

[59] Prehearing Memorandum of the Recording Industry Association of America, CRT Docket No. 80-2 [hereinafter "RIAA Memorandum"] at 1.

[60] RIAA Memorandum at 26-27.

In sum, a new royalty tax obviously cannot be justified on the grounds that it will aid struggling composers and artists, for whatever small benefit this group would receive from such a tax would be insignificant in comparison to the millions of consumer dollars that the big six recording companies, the established publishing companies, and a few singer/songwriters would receive.[61] Since there is thus no reasonable prospect that a home audio taping levy would promote creative activity, and since there is no evidence that today's level of musical creation is too low,[62] Congress should once again reject the industry's attempt to tax home tapers.

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[61] Also, there would be nothing to stop a record company or music publisher from using the cash flow from a royalty tax to fund the purchase of a cable TV network, department store chain, etc. Rather than spur creativity, a royalty tax could have the opposite effect, turning the music business into a "cash cow" to fund conglomerate acquisitions.

[62] The RIAA advised the Copyright Royalty Tribunal in 1980 that "there is no dearth of available musical compositions." RIAA Memorandum at 37.

CBS ANNUAL REPORT FOR 1983

CBS/Records Group

Dollars in millions

	1983	1982	1981	1980	1979
REVENUES	$1,158.8	$1,056.1	$ 795.3	$1,105.6	$1,257.1
OPERATING PROFITS	$ 109.4	$ 22.1	$ 58.9	$ 71.3	$ 68.4

The results of the Group's home video operations are not reflected in the table above. They are included in "Other" in the business segment information on pages 46 and 47.

The CBS/Records Group firmly reasserted its position as the leading U.S. music company during 1983, translating a moderate sales increase into a dramatic surge in operating profits. In a domestic marketplace that grew only slightly and an international marketplace that hardly grew at all, the Group consistently outperformed the music industry as a whole, fueled by an unusually varied mix of best-selling recordings by established stars and by newcomers from the United States and around the world. Certainly the most notable among these was Michael Jackson's *Thriller*, by far the best-selling album in CBS/Records Group history.

The Group's 1983 performance benefited from the upturn in the U.S. economy and the declining impact of video games on consumers' disposable income. More importantly, the Group reaped the rewards of the costly but essential operational streamlining and restructuring effected in recent years. Although serious obstacles remain, chief among them the unabated impact of home taping and of foreign exchange losses caused by the continuing strength of the U.S. dollar against foreign currencies, the Group is now positioned to maintain solid profitability in a mature world market with only modest short-term growth prospects.

The CBS Records Division, the Group's domestic recorded music operation, rebounded strongly from the industry's 1982 difficulties with improved revenues, and a sizable operating profit as opposed to a loss in 1982. At the same time, it continued its vigorous efforts to reduce costs and further refine manufacturing and marketing techniques.

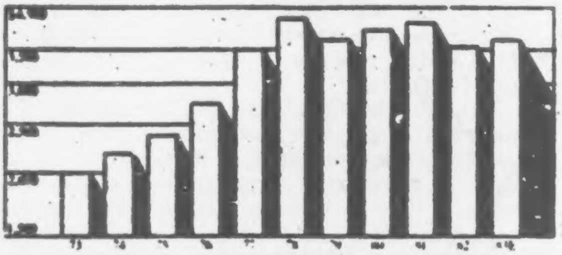
Gains in unit sales by the CBS Records International Division were more than offset in 1983 by the continued worldwide strength of the U.S. dollar and by currency devaluations affecting a number of the Division's large subsidiaries, leading to a decline in total sales reported in dollars. Nevertheless, a number of key subsidiaries around the world enjoyed significant revenue and profit growth. Like its domestic counterpart, CBS Records International has achieved major improvements in operating efficiency and, as a result, was able to increase its profits despite lower sales. As the Division continues to develop recording artists for its own markets, it grows stronger as a vital source of new artists for the domestic division and the U.S. market.

The Columbia House Division had an exceptional year in 1983, as its music clubs achieved record-high enrollments of new members and the largest total membership in the Division's history. On a moderate sales increase, Columbia House achieved a sizable increase in operating profits, the result of its marketing efforts and operational advantages gained through a highly cost-effective computerization program.

With the addition of the MGM/United Artists catalogs of music copyrights, CBS Songs became one of the three largest worldwide music publishers, and increased both sales and operating profits.

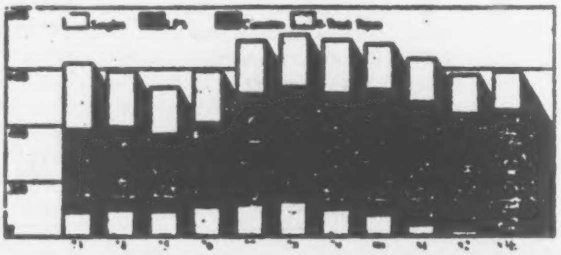
Masterworks, the Group's classical music operation, substantially improved its profitability during the year, and continued the dramatic improvement in its U.S. market position that began in 1980. The label's management of its artists and selection of repertoire have been sharpened, with the result that Masterworks' top-selling albums have achieved significantly higher sales than in the past. Perhaps the best measure of the Masterworks label's success in 1983 was the three awards received from *Billboard* magazine, the record industry's leading trade publication, for best classical label, best classical album and best artist.

In 1983, the Records Group began distribution of Compact Discs, which use a new recording technology that provides the most significant advance in home audio quality since the introduction of the 12-inch LP by CBS in 1948. The Compact Disc is a small (4¾-inch diameter) disc with a highly reflective surface which is "read" by a laser beam in a special player. The audio signal on the disc is digitally recorded, allowing a wide dynamic range, a high signal-to-noise ratio, improved channel separation and a flat frequency response across the entire audible range. Under an agreement reached in 1983 between CBS and Sony Corporation of Japan, Compact Discs will be manufactured by the Digital Audio Disc Corporation, a U.S. subsidiary of CBS/Sony, Inc. Production will begin in 1984 in Terre Haute, Indiana.



U.S. Recording Industry Sales

Source: Recording Industry Association of America, Inc. and CBS Economic Analysis



U.S. Recording Industry Sales

Source: Recording Industry Association of America, Inc. and CBS Economic Analysis

In a year that saw music video grow tremendously as a promotional tool and a potential profit generator, the Group continued its leadership in this field with the creation of the CBS Video Enterprises Music Video Programming unit, which has been charged with maximizing the Group's return on its investment in video.

CBS RECORDS DIVISION

Reversing a four-year trend of declining unit shipments and weakening retail sales, the U.S. recorded music industry had a small but encouraging upturn in 1983. While not a return to the boom years of the late 1970's, this is evidence that the industry is recovering from the impact of economic recession and new home entertainment technologies.

CBS Records led the industry with an extraordinarily broad range of best-selling recordings. Michael Jackson's album *Thriller*, with worldwide sales so far of more than 27 million units, headed the *Billboard* album chart for most of 1983, and albums by such superstar artists as Billy Joel, Journey, Barbra Streisand, Culture Club and Quiet Riot also have sold more than a million units each, enabling the Division to far exceed the small industry growth rate.

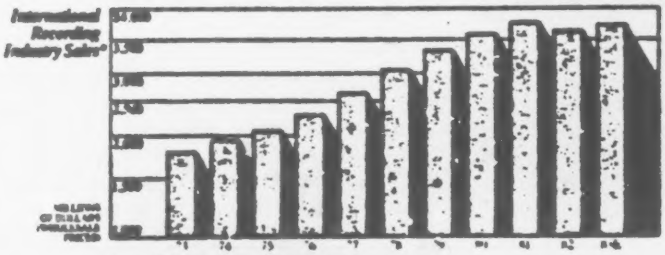
Almost as striking as the volume of these sales was the variety of sources from which they came. Artists signed by CBS Records International or by the CBS Associated Labels–Men at Work, Bonnie Tyler, Loverboy, Julio Iglesias, Quiet Riot–augmented a steady flow of hits from the Columbia and Epic labels. As American musical tastes become more diverse, CBS Records' extensive repertoire is uniquely positioned for success.

On a healthy increase in sales, the Division was able to turn 1982's net operating loss into a substantial operating profit in 1983. A key factor in this profit performance was the recently enhanced cost-efficiency of the Division's manufacturing and marketing operations, which has greatly lowered the Division's break-even point. Perhaps most significant among these changes has been the consolidation and modernization of the Division's prerecorded audio cassette facilities in Carrollton, Georgia. In 1983, cassettes reached virtual parity with 12-inch discs in total industry unit sales, and could account for as much as 60 percent of unit sales by the end of 1984.

In music video, CBS Records remained the industry leader during 1983, supplying more promotional videotapes than any other company to cable television's MTV–Music Television–and becoming the first in the industry to receive license fees for television use of music videos–from the NBC *Friday Night Videos* program. The Division also began to package promotional and concert videos for sale to pay cable services, television stations and on videocassette and videodisc.

The most serious of the Division's problems, however, moved no closer to resolution in 1983. Home taping continues to drain hundreds of millions of dollars from the music industry, and although CBS Records continues to press for legislative protection, in early 1984 such protection did not seem near at hand.

CBS RECORDS INTERNATIONAL DIVISION



Source: CBS Records International estimate
*CBS-Served Markets

Best-seller charts in the United States and around the world testify to 1983's most significant musical trend: a shift from national to international repertoire. Artists recording in English and Spanish now cross national boundaries with ease, and those recording in other languages may not be far behind.

This development has been particularly beneficial to CBS Records International, with its 36 wholly owned companies, six joint venture companies and 10 licensees. Where once the Division drew most of its revenues from international sales of U.S. repertoire, it has now established strong local artists in most of its territories and is providing an increasing number of best-selling recordings to world markets. American artists naturally continue to play a key role in the Division's success–Michael Jackson, Billy Joel and Toto each had major international hits in 1983. The recent success in the United States of such Division artists as Loverboy (Canada), Bonnie Tyler and Adam Ant (United Kingdom) and Men at Work (Australia) has also been substantial. Julio Iglesias, the Division's best-selling artist, made his debut in English in 1983, and has already attracted a large American audience through concert and television appearances.

The Division's operations in Canada, Japan and continental Europe enjoyed substantial growth in 1983. Unfortunately, some of the territories in which CBS Records International continues to have its greatest successes in developing local repertoire–nations such as Brazil and Mexico–have also been the scene of the Division's most severe foreign exchange losses. While those losses remain largely beyond the Division's control, CBS Records International has continued its efforts to reduce overhead and improve manufacturing efficiency. The capital improvement plan of recent years is now nearly completed, and plants in many countries have been modernized and expanded.

COLUMBIA HOUSE DIVISION

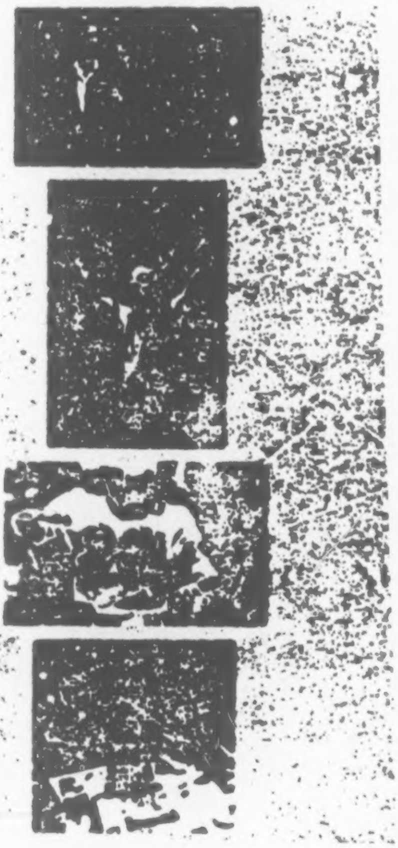
With highest-ever totals in new member enrollments and year-end membership, the Columbia Record and Tape Clubs and their Canadian counterparts led Columbia House to a near-record oper-

	1983	1982	1981	1980	1979
	(Dollars in millions)				
CBS/Broadcast Group	$2,389.4	$2,165.2	$1,921.1	$1,701.4	$1,525.5
CBS/Records Group	1,158.8	1,066.7	1,218.3	1,338.0	1,287.1
CBS/Publishing Group	587.0	538.7	507.7	486.6	399.8
CBS/Columbia Group	342.7	308.5	253.0	271.5	257.0
Other	67.6	51.0	61.5	59.1	37.9
Elimination of Intergroup Revenues	(5.3)	(7.3)	(5.7)	(4.6)	(6.4)
Total Revenues	**$4,540.2**	**$4,122.8**	**$3,955.9**	**$3,852.0**	**$3,500.9**
Foreign	$ 642.1	$ 664.5	$ 721.2	$ 753.8	$ 653.3
Domestic	3,898.1	3,458.3	3,234.7	3,098.2	2,847.6

	1983	1982	1981	1980	1979
	(Dollars in millions)				
CBS/Broadcast Group	$291.5	$270.8	$316.9	$247.1	$269.3
CBS/Records Group	109.4	22.2	58.9	72.3	68.4
CBS/Publishing Group	55.2	38.0	43.1	45.0	42.7
CBS/Columbia Group	(15.7)	3.2	11.1	24.5	24.3
Other	(29.8)	(24.0)	(22.8)	17.0	19.3
Operating Profits	**$410.6**	**$310.2**	**$407.2**	**$405.9**	**$424.0**
Foreign	$ 69.8	$ 64.9	$ 71.7	$ 72.2	$ 68.0
Domestic	340.8	245.3	335.5	333.7	356.0

We are unique among companies of our size in deriving virtually all our revenue from human creativity rather than material resources–from what people write, what they compose and what they perform–and from products which further human expression and development.

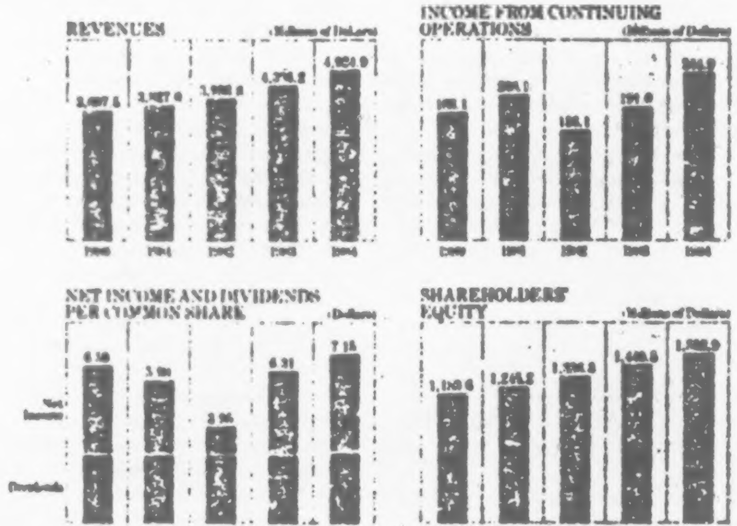
1984 CBS ANNUAL REPORT



TO OUR SHAREHOLDERS

We are pleased with the Company's splendid performance in 1984. CBS's financial results—income from continuing operations, net income and revenues—were at the highest levels in the Company's history. Our investment in new and expanded product and service lines was also at the highest level. We achieved this success by paying close attention to our customers and our costs, and by improving the quality of our products and services. The statement on this Report's cover—our creative credo at CBS—first appeared in the Annual Report of 1976; it captures what we see as the special character of CBS. We are proud that the creative quality of our products reached new highs in 1984, and the consonance with our financial results is both natural and reassuring.

Our largest business, the CBS/Broadcast Group, completed a year of success unparalleled in the history of the industry. For the first time ever, a network outperformed its competition in the four major dayparts—prime time, evening news, daytime and late night—that encompass the television day. Our second largest business, the CBS/Records Group, produced the highest income of any company in the history of its industry. In both businesses, these successes were accompanied by important product and service quality breakthroughs. We find it reassuring that these successes reconfirm so elegantly the validity of the historic CBS commitment to maintain-



CBS FIVE-YEAR FINANCIAL SUMMARY

CBS/RECORDS GROUP

The CBS Records Group enjoyed a second consecutive banner year in 1984, with profits for the Group as a whole, and for the CBS Records and Columbia House Divisions, climbing to their highest levels ever. The Group's profits continued to increase at a substantially faster rate than sales, underscoring the effectiveness of ongoing efforts to reduce costs and maximize operating efficiency. Perhaps the most encouraging aspect of the Group's success was that it was fueled by a long list of new, developing and established artists from across the musical spectrum and from all over the world.

The Group maintained its leading position in the global marketplace which was characterized by a vigorous domestic recorded music market and slower-growing international markets. The greatest obstacle to industry growth worldwide remained the unauthorized reproduction of copyrighted recordings, a problem which grows in complexity as new audio and video technologies reach the marketplace.

For the CBS Records Division, the Group's domestic recorded music operation, 1984 was a year of record revenues and profits. During the year, domestic manufacturing operations were reorganized as a separate unit, CBS Records Group-Operations (U.S.), with the goals of improving service, productivity and product quality.

Unit sales for the CBS Records International Division rose again in 1984, but the continued strengthening of the dollar against foreign currencies kept Division revenues at approximately 1983 levels. Although overall profits declined, a number of the Division's territories reported substantial improvement in profit performance from the prior year.

The Columbia Record and Tape Clubs in the United States and Canada increased their total memberships in 1984 with resultant increases in profits and revenues for the Columbia House Division, the Group's direct marketing arm.

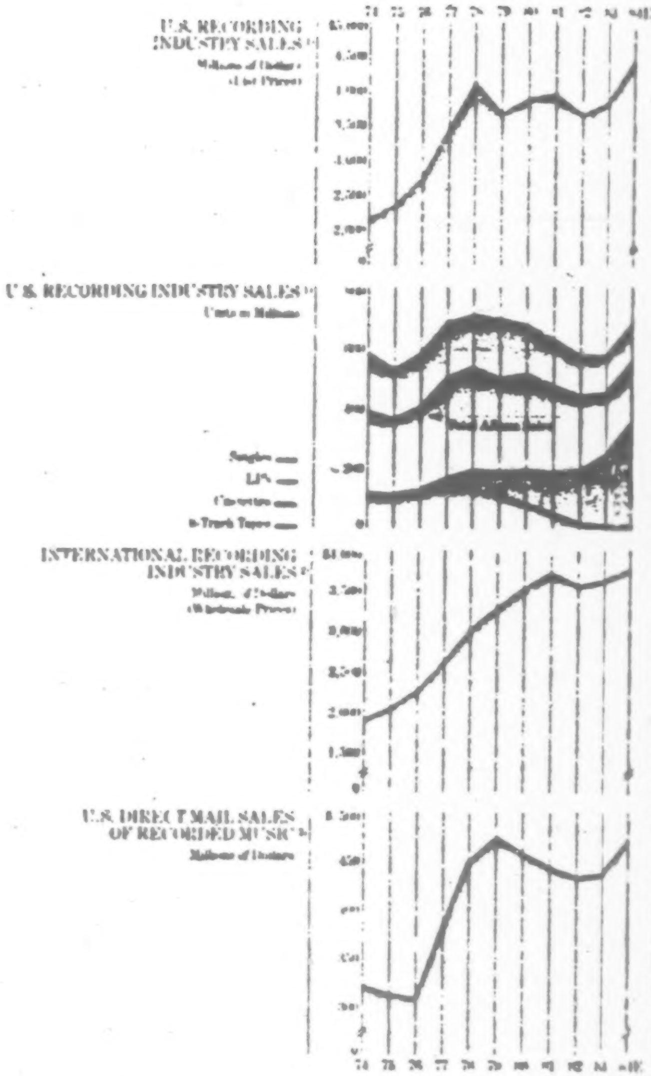
Revenues in 1984 for CBS Songs, the Group's music publishing division, held at the same level as 1983, but profits declined due to a non-recurring gain in 1983 from the sale of print rights from the MGM/UA song catalogs. Excluding this 1983 gain, the Division's 1984 profits increased substantially over those of 1983.

For the second year in a row, Masterworks was named Classical Record Label of the Year by *Billboard* magazine, a reflection of the increasing prestige of the Records Group's worldwide classical music operations. In December, Masterworks named Isaac Stern its first Artist Laureate, and signed the distinguished

Dollars in millions

CBS/RECORDS GROUP FINANCIAL SUMMARY

1984	1983	1982	1981	1980
Revenues				
$1,265.1	1,158.8	1,066.7	1,218.3	1,330.0
Operating Profits				
$ 123.5	109.1	22.2	54.9	72.3



In 1984, the domestic recorded music industry continued to build on the growth it resumed in 1983. Estimated industry sales gains of 17 percent reflected the enthusiasm infused by the music video phenomenon, the popularity of new artists as well as the ongoing national economic rebound.

For the second year in a row the music cassette surpassed the LP as the consumer's format of choice. Growing at an average annual rate of roughly 33 percent in recent years, the cassette's popularity can be attributed in part to its convenience, durability and portability.

At the international level, as measured in CBS-served markets, the industry achieved its highest sales ever. For U.S.-based record companies, however, the weakness of foreign currencies when converted to U.S. dollars continued to restrain revenue growth.

Direct mail marketing remains an important distribution channel for the industry. In 1984, improved marketing strategies, excitement generated by the music industry itself and a strong economy served to boost industry sales over 8 percent.

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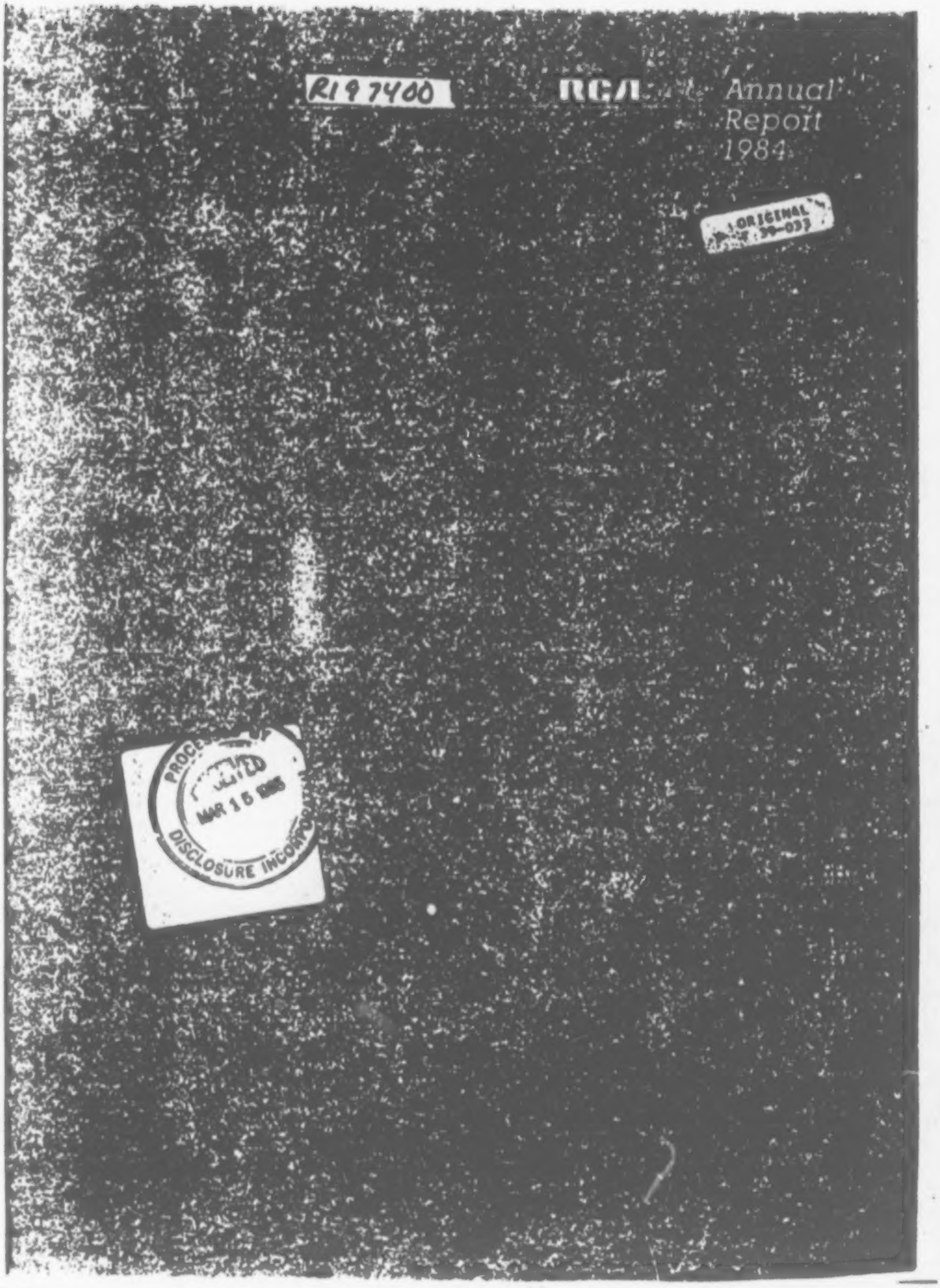
(1)Source: Recording Industry Association of America, Inc. and CBS Economic Analysis
(2)Source: CBS Records International and CBS Economic Analysis estimate
(3)Source: Columbia House Division and CBS Economic Analysis



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RCA Annual Report 1984

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Entertainment. RCA is reporting a new industry segment, Entertainment, beginning in 1984 because each of the products and services included therein—broadcasting, audio records and prerecorded tapes, and video software—provides a similar entertainment-oriented software product to the consumer. The management of RCA considers this segment to be one of the core businesses of the company and believes this presentation will further improve RCA's financial reporting.

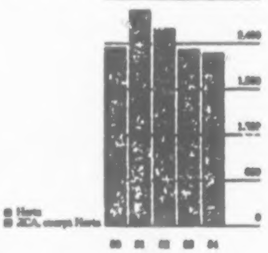
The Broadcasting (NBC) subsegment reported record sales and earnings in 1984. Sales increased by 13 percent in 1984 to $2.37 billion from the prior year's level of $2.09 billion. Pretax earnings in 1984 amounted to $218.1 million—an increase of 40 percent from 1983. All of NBC's operating units had higher profits in 1984. The Television Network advanced to a second-place finish in the prime-time November sweeps and held them in that position through the end of the year. It was first in prime time among key demographic groups—viewers considered to have the most appeal to advertisers. Improvements were also made in Daytime and Late Evening. In 1984, the increased profitability resulting from improved performance and demographics more than offset the substantial and unusual expense associated with broadcasting two political conventions and the election campaigns. In 1984, the Television Stations Division reported record sales and earnings for the fifth consecutive year. In 1983, sales increased 17 percent and pretax earnings increased 46 percent over 1982 as a result of improved demographics and strong advertiser demand for the Television Network and Television Stations Division as well as expanded services and a larger audience for the Radio Division.

The Records and Video subsegment consists of RCA Records and the joint ventures with Columbia Pictures Industries, Inc. to distribute home video software. The joint ventures are accounted for on an equity basis; therefore, their sales are not consolidated, and RCA reports only its share of their pretax profits. In 1984, sales of RCA Records increased 4 percent to $621.8 million, primarily as a result of higher record club volume. Earnings for this subsegment increased in 1984 because of the improved profitability of the joint ventures, which more than offset higher artist investment and the start-up costs of a new audiocassette manufacturing facility at RCA Records. The joint ventures' improved profits were a result of increased worldwide demand for VCRs, which brought new consumers into the marketplace for prerecorded video tapes, and increased penetration into new foreign markets. In 1983, sales of RCA Records were up 2 percent as higher unit volumes were largely offset by weakening foreign currencies. RCA Records' profits in 1983 improved as a result of higher unit volume and strong cost controls. Earnings for the joint ventures were significantly higher in 1983 as a result of the ventures' emergence from a start-up situation in 1982 to a full year of operations and the increase in VCR owners.

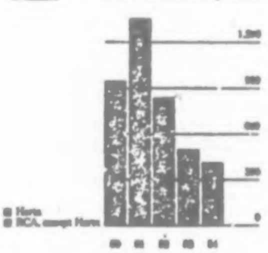
Communications. Revenues in 1984 increased by 11 percent to a new high of $117.2 million. This resulted from new installations of commercial leased facilities and increased satellite-transponder usage at RCA Americom, increases in international and domestic telex volume at RCA Globcom, and a higher volume of installed circuits by RCA Cylix. Earnings for the Communications segment increased by 12 percent to $107.0 million primarily as a result of this additional volume. In 1984, RCA Cylix continued to report start-up losses comparable with the 1983 level. In 1983, revenues increased by 18 percent, reflecting strong growth in RCA Americom's commercial leased facilities and increased satellite-transponder capacity. Earnings for the Communications segment in 1983 were lower than in the 1982 period as a result of higher start-up losses at RCA Cylix and the absence of the prior year's nonrecurring gains from the sale of transponders, the sale of tax attributes, and the sale of the Satcom V satellite to Alascom, Inc. Excluding these 1982 nonrecurring gains, 1983 earnings were 10 percent higher.

Transportation Services. Revenues from continuing businesses in 1984 were a record $1.44 billion, or 7 percent above 1983, reflecting new highs in car-rental transactions for both domestic and international operations and higher revenues from the construction equipment-rental business offset by lower car-leasing revenues. Earnings in 1984 on a comparative basis, after the change in accounting for investment tax credits, were essentially unchanged from 1983. Profit improvements from increased car rentals were recorded in Hertz' European operations, as increased vacation travel from the United States resulted from the strengthening of the U.S. dollar. Hertz' construction equipment-rental business had higher profits in 1984, as higher volume of transactions and firmer pricing levels resulted from a rebounding construction industry. Car-rental operations in

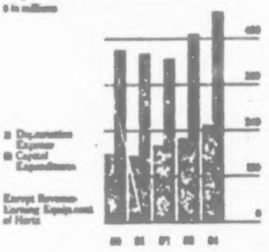
Total Debt
$ in millions



Interest-Sensitive Debt
$ in millions



Capital Expenditures and Depreciation Expense
$ in millions



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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended June 30, 1985	Commission file number 1-978

RCA CORPORATION

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	13-1194630 (I. R. S. Employer Identification No.)
30 Rockefeller Plaza, New York, New York (Address of Principal Executive Offices)	10020 (Zip Code)

(212) 621-6000
Registrant's telephone number, including area code

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Not applicable
Former name, former address and former fiscal year, if changed since last report.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X . No___.

The number of shares outstanding of the registrant's common stock is 82,457,788 shares as of June 30, 1985.

This document consists of 17 pages.
Exhibit index is on page 14.

RCA CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE RESULTS OF OPERATIONS AND FINANCIAL CONDITION—(Continued)

Consumer Products and Services subsegment sales decreased 15% and 11% in the second quarter and first six months of 1985 compared to the same periods last year. These decreases reflect the severe price competition in television receivers and video cassette recorders that began in the second half of 1984 and the decrease in VideoDisc sales as a result of the phase-down of operations, partially offset by an increase in service revenues. Earnings for the second quarter of 1985 decreased 23% compared to last year and decreased 12% for the first half of 1985 compared to the same period in 1984 (before the provision for the VideoDisc restructure but including VideoDisc losses of $17.1 million pretax). Within this subsegment, the Consumer Electronics division earnings were down for the second quarter and first six months of 1985 compared to the same prior year periods as pricing pressures decreased operating margins.

Commercial Products and Services subsegment sales decreased 2% and 4%, respectively, for the second quarter and first half of 1985 compared to 1984. The decreases primarily reflect the continued decline in the Solid State division, partially offset by an increase in the commercial satellite business in Aerospace and Defense. Earnings for this subsegment declined 16% and 18% for the three and six months ended June 30, 1985, respectively, compared to 1984, primarily reflecting reduced demand for semiconductors and the resultant excess capacity at the Solid State division.

The Government Systems and Services subsegment had record sales for the second quarter and first half of 1985, reflecting 10% and 9% increases, respectively, over the same prior year periods. Earnings for this subsegment rose 14% for both the three and six month periods ended June 30, 1985 compared to last year. During the second quarter, the subsegment received two major contracts for work on the nation's Space Station program.

In the Entertainment segment, Broadcasting (NBC) sales increased 13% and earnings rose 43% in the second quarter of 1985 compared to the same period in 1984. Sales in the first six months of 1985 were 14% higher than in 1984, and earnings increased 68%. The improved sales and earnings are primarily attributable to the performance of the Television Network in prime time. The strength of its regular prime-time schedule put NBC on top during the important May rating (sweeps) period with both the Nielsen and Arbitron services. NBC's top ranking in total homes and in key demographic groups continued in the month of June. In the Records and Video subsegment, sales increased 15% and 6% for the second quarter and first half of 1985 compared to the same periods last year. Earnings increased significantly for the second quarter and first six months of 1985 compared to the same periods in 1984. These increases reflect the success of new domestic audio releases and strong performance of RCA's domestic joint venture with Columbia Pictures.

The Communications segment reached record sales with increases of 3% in the second quarter and 4% in the first six months of 1985 over the same periods in 1984. Operating profits were down for the second quarter and first half of 1985, respectively, compared to the same 1984 periods. RCA Global Communications, Inc. continued its growth in the domestic telex market and maintained its leadership position in leased channels and international telex.

The Transportation Services segment (Hertz) reported record revenues in the second quarter and first six months of 1985 compared to last year, reflecting 5% and 3% increases, respectively. The revenue increases are primarily due to continued high transaction levels in its car-rental and construction equipment rental and sales operations. Hertz' earnings decreased substantially in the second quarter and first six months of 1985, reflecting a highly competitive pricing environment in the domestic car-rental business and continued softness in the vehicle resale markets.

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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OF
THE SECURITIES EXCHANGE ACT OF 1934

70
EX 29

For the fiscal year ended December 31, 1984 — Commission file number 1-4243

MCA INC.

(Exact name of Registrant as specified in its charter)

Delaware	95-2011468
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 Universal City Plaza Universal City, California	91608
(Address of principal executive offices)	(Zip Code)

818-985-4321
(Registrant's area code and telephone number)

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Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common stock, no par	New York Stock Exchange Pacific Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes ✓ No _

As of January 31, 1985, 48,795,330 shares of MCA INC. common stock were outstanding, excluding shares held by MCA INC. as treasury stock. The aggregate market value of MCA INC. common stock held by nonaffiliates (based on the closing price at January 31, 1985 on the New York Stock Exchange — Composite Transactions) was approximately $1,671,000,000. All officers, directors and more than 5% stockholders of Registrant are deemed "affiliates" of Registrant for the purpose of calculating such aggregate market value. Registrant, however, does not represent that such persons, or any of them, would be deemed "affiliates" of Registrant for any other purpose under the Securities Exchange Act of 1934 or the Securities Act of 1933.

DOCUMENTS INCORPORATED BY REFERENCE

(Specific information incorporated is indicated under the applicable item herein)

Document	Incorporated By Reference in Part Number
Registrant's 1984 Annual Report to Shareholders for the Year Ended December 31, 1984 (1984 Annual Report)	I, II
Registrant's Proxy Statement for the Annual Meeting of Stockholders to be held May 7, 1985 (Proxy Statement)	III

TOTAL OF SEQUENTIALLY NUMBERED PAGES 72
Exhibit Index on Sequentially Numbered Page 29

MCA INC. and Subsidiaries

Consolidated Statement of Income

($ in thousands)	1984	1983	1982
Revenues			
Filmed entertainment	$ 888,851	$ 926,969	$1,005,801
Records and music	255,930	188,104	165,933
Retail and mail order	310,638	287,948	247,566
Book publishing	116,842	106,214	90,063
Other operations	78,981	75,304	76,659
	1,651,242	1,584,539	1,586,022
Costs and Expenses of Operating Divisions			
Filmed entertainment	827,263	763,191	792,700
Records and music	247,091	196,078	141,707
Retail and mail order	304,058	268,658	235,229
Book publishing	106,808	99,326	84,593
Other operations	69,428	72,588	83,344
	1,554,648	1,399,841	1,337,573
Operating Income (Loss) of Divisions			
Filmed entertainment	61,588	163,778	213,101
Records and music	8,839	(7,974)	24,226
Retail and mail order	6,580	19,290	12,337
Book publishing	10,034	6,888	5,470
Columbia Savings	—	—	(5,506)
Other operations	9,553	2,716	(1,179)
	96,594	184,698	248,449
Not Allocated to Divisions			
Corporate general administration	15,125	15,531	16,328
Investment income	(20,568)	(32,293)	(41,577)
	(5,443)	(16,762)	(25,249)
Income before taxes	102,037	201,460	273,698
Income taxes	7,100	54,300	97,500
Net Income	$ 94,937	$ 1[illegible]	$ 176,198
Earnings Per Share	$ 1.96	$ [illegible].06	$ 3.69

The accompanying notes are an integral part of these consolidated financial statements.

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FORM 10-Q
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Quarterly Report Under Section 13
of the Securities Exchange Act of 1934

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For Quarter Ended: June 30, 1985

Commission file number: 1-4243

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MCA INC.
(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

95-2011468
(I.R.S. Employer Identification No.)

100 Universal City Plaza, Universal City, California
(Address of principal executive offices)

91608
(Zip code)

Area Code 818 - 985-4321
(Registrant's telephone number)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days. Yes X No __

As of July 31, 1985, 49,539,015 shares of MCA INC. common stock were outstanding, excluding shares held by MCA INC. as treasury stock.

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TOTAL PAGES 24

MCA INC. and Subsidiaries

CONSOLIDATED STATEMENT OF INCOME - UNAUDITED
($ in thousands)

	Three Months Ended June 30		Six Months Ended June 30	
	1985	1984	1985	1984
REVENUES				
Filmed entertainment	$229,014	$181,773	$486,987	$406,042
Records and music	65,225	60,743	128,297	116,293
Retail and mail order	53,974	56,115	119,370	129,421
Book publishing	33,511	28,526	63,109	56,651
Other operations	34,658	22,032	50,188	33,223
	416,382	349,189	847,951	741,630
COSTS AND EXPENSES OF OPERATING DIVISIONS				
Filmed entertainment	217,726	166,357	456,578	369,736
Records and music	61,610	59,231	120,696	112,627
Retail and mail order	59,057	60,078	129,956	134,499
Book publishing	29,901	26,327	55,870	51,360
Other operations	30,670	20,379	45,173	32,681
	398,964	332,372	808,273	700,903
OPERATING INCOME (LOSS) OF DIVISIONS				
Filmed entertainment	11,288	15,416	30,409	36,306
Records and music	3,615	1,512	7,601	3,666
Retail and mail order	(5,083)	(3,963)	(10,586)	(5,078)
Book publishing	3,610	2,199	7,239	5,291
Other operations	3,988	1,653	5,015	542
	17,418	16,817	39,678	40,727
NOT ALLOCATED TO DIVISIONS				
Corporate general administration	3,526	2,391	7,034	5,980
Investment income	(4,693)	(4,806)	(8,572)	(10,040)
Interest expense	1,987	779	3,041	1,602
	820	(1,636)	1,503	(2,458)
Income before taxes	16,598	18,453	38,175	43,185
Income tax provision (credit)	4,300	(1,500)	7,500	2,200
NET INCOME	$ 12,298	$ 19,953	$ 30,675	$ 40,985
EARNINGS PER SHARE	$ .25	$ .42	$ .63	$ .85
PRO FORMA EARNINGS PER SHARE AFTER STOCK SPLIT	$ .17	$ .27	$ .42	$ .56
DIVIDENDS PER SHARE PRIOR TO SPLIT	$ .22	$ .22	$ .44	$ .44

The accompanying notes are an integral part of these unaudited consolidated financial statements

MCA INC. and Subsidiaries

CONSOLIDATED BALANCE SHEET - UNAUDITED
($ in thousands)

	June 30 1985	December 31 1984	June 30 1984
ASSETS			
CURRENT ASSETS			
Cash and short term investments	$ 214,202	$ 167,024	$ 147,216
Receivables, less allowances of $54,870, $55,431 and $49,397	337,417	317,603	298,662
Film costs, net of amortization	261,937	230,576	221,774
Inventories	120,191	117,305	117,788
Prepaid expenses	71,156	55,192	52,795
	1,004,903	887,700	838,235
NONCURRENT ASSETS			
Film costs, net of amortization	464,533	439,872	384,466
Television license fees receivable	110,306	105,399	113,997
Investment in unconsolidated companies	32,264	33,398	33,540
Deferred charges and other assets	128,663	98,337	97,114
	735,766	677,006	629,117
PROPERTY, PLANT AND EQUIPMENT, at cost			
Land	28,412	28,370	28,054
Buildings and leasehold improvements	377,387	362,260	344,231
Furniture, fixtures and equipment	180,092	170,264	161,582
	585,891	560,894	533,867
Accumulated depreciation	(196,450)	(181,858)	(170,784)
	389,441	379,036	363,083
	$2,130,110	$1,943,742	$1,830,435

The accompanying notes are an integral part of these unaudited consolidated financial statements

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company's overall financial condition as of June 30, 1985 remains strong. Working capital was $477 million at June 30, 1985 compared to $459 million and $413 million at December 31, 1984 and June 30, 1984, respectively. Cash and short term investments were $214 million at June 30, 1985 compared to $167 million and $147 million at December 31, 1984 and June 30, 1984, respectively. The Company's current strong financial condition, along with its available line of credit, is more than adequate to meet current obligations and commitments.

The Filmed Entertainment Division's revenues increased for the three and six months ended June 30, 1985 primarily due to (1) increased second quarter theatrical revenues resulting from Fletch, Brewster's Millions, Mask and The Breakfast Club; (2) increased television revenues from the increased number of television programs licensed to networks and increased licensing for domestic syndication, both primarily in the first quarter of 1985; (3) increased Home video and pay television revenues, primarily from the increased number of videocassettes sold; and (4) increased Studio Tour and Amphitheatre revenues. The above were offset somewhat by decreased Merchandising revenues. The Records and Music Group's revenues increased for both periods primarily due to increased MCA record label sales, offsetting distributed product sales decreases. The Book Publishing Division's revenues increased due to the success of new releases. The Retail and Mail Order Division's revenues decreased for both 1985 periods primarily due to scheduled lower catalog mailings and the elimination of certain catalogs.

The Filmed Entertainment Division's operating income decreased for the three and six months of 1985 primarily due to the disappointing results of several theatrical films released during the second quarter of 1985 by the Universal Pictures division and due to the significantly lower Merchandising revenues in the first quarter, partially offset by the increased Television, Home video and Studio Tour and Amphitheatre results in both periods of 1985. The Records and Music Group's operating income substantially increased due to increased revenues as discussed above. The Book Publishing Division's operating income increased due to increased revenues as discussed above. Other Operations reported increased operating income for both the three and six months of 1985

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WARNER COMMUNICATIONS INC.

1984 ANNUAL REPORT

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WARNER COMMUNICATIONS INC. IS A COMPANY WHOSE MOST IMPORTANT ASSETS ARE PEOPLE--THE CREATIVE INDIVIDUALS WHOSE TALENTS ARE EVIDENT IN EVERY MOTION PICTURE AND TELEVISION SERIES WE PRODUCE, EACH MUSICAL RECORDING WE RELEASE, EVERY BOOK AND MAGAZINE WE PUBLISH, AND EACH CABLE PROGRAMMING SERVICE WE DELIVER. » WE HAVE CHOSEN TO FEATURE A FEW OF THOSE PEOPLE IN THIS YEAR'S ANNUAL REPORT AS A MEASURE OF THE RESPECT WE HAVE FOR THEIR ABILITIES. » WE HAVE ALSO DONE SO TO CAST LIGHT ON THE UNIQUE NATURE OF THE BUSINESSES IN WHICH WE PLAY A LEADING ROLE. »

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LETTER TO SHAREHOLDERS

For Warner Communications, 1984 was a year of profound change. It was also a year that, from the vantage point of early 1985, established a firm foundation for renewed profitable growth.

Your Company's major continuing businesses turned in exceptional performances in 1984. WCI's filmed entertainment division achieved record operating income of $150.4 million, an increase of 38% over the preceding year. Our recorded music division rebounded dramatically from several weak years, reporting operating income of $89.6 million—just short of 1978's all-time high. Publishing revenues set a record and operating income of $16.0 million was near an all-time peak.

For the year, WCI reported income from continuing operations of $13.1 million, or $.12 per share, compared to a 1983 loss of $11.0 million, or $.17 per share, proof of your Company's operating strength and an indicator of future profitability. Revenues of $2.0 billion exceeded 1983's comparable results by 17%.

WCI's net loss of $586.1 million, or $9.73 per share, in 1984 was primarily due to first half operating losses at Atari, the disposition on July 2 of Atari's home computer and home video game operations, and management's decision in the fourth quarter to account for the remaining $150 million of notes and warrants of the new Atari Corp. on the more conservative cash basis and no longer carry them on our balance sheet. Additional losses were recorded from the write-down of other discontinued businesses.

The performance of our ongoing operating divisions in 1984 deserves special attention and provides the basis for our confidence. Important highlights of the year include:

☐ Our Filmed Entertainment division generated all-time high revenues of more than $1 billion. Operating income increased 36% over 1979's previous high.

☐ Warner Bros. was the motion picture industry's top performer at the boxoffice in 1984. Domestic film rentals of $305 million established a new high for the company.

☐ Warner Bros. Television Distribution achieved record results thanks in part to the highly successful syndication of the WB-TV series *The Dukes of Hazzard*.

☐ Warner Home Video reported its best year ever, with revenues increasing significantly over 1983 figures.

☐ WCI's Recorded Music division achieved all-time high revenues and a 48% increase in operating income.

☐ Warner Bros. Records had its best year, highlighted by Prince's *Purple Rain*, which set a company record with worldwide sales in one year of almost 11 million units.

☐ WEA Corp. achieved new highs in both its prerecorded music and home video distribution segments.

☐ Warner Bros. Music reported record revenues and operating income, surpassing 1983's previous marks.

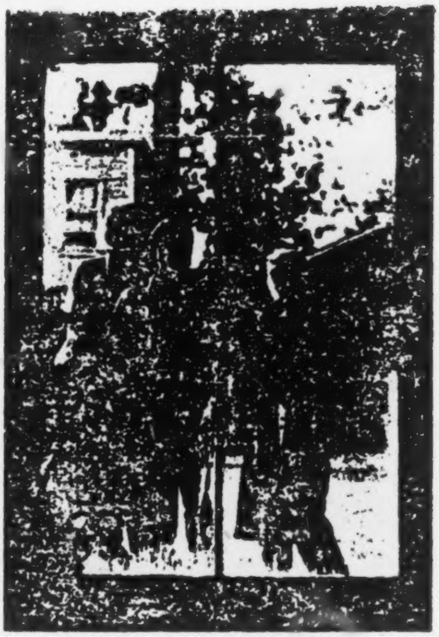
☐ Warner Books attained new highs for revenues and operating income for the third consecutive year.

☐ Warner Amex reduced its debt to $550 million from $852 million at the end of 1983 while pre-tax losses were cut 37%.

☐ MTV Networks completed a successful initial public offering of 34% of its capital stock, realizing net proceeds of more than $70 million. *MTV: Music Television* and *Nickelodeon* continued to register impressive subscriber gains and a new video music service, *VH-1*, was launched.

☐ BHC showed revenue and operating income growth.

☐ Showtime/The Movie Channel reported substantial gains in revenue and operating income in its first full year as a joint venture.



Lone Justice; Don Heffington, Marvin Etzioni, Ryan Hedgecock, Maria McKee

▲ The resurgence of the record industry has been partially attributed to the emergence of new talent. In 1985, Geffen Records will issue Lone Justice's first album. The band has received acclaim for its live performances and its Geffen release promises to be one of the year's most exciting debuts.

films—including *Sudden Impact*, *The Right Stuff*, *Greystoke* and *Never Say Never Again*—sold well. With the expanding population of VCR users and a strong slate of 1985 releases such as *Police Academy*, *Gremlins* and *Tightrope*, WHV should again experience substantial growth in 1985.

WEA International, WCI's overseas recorded music and home video distribution operation, saw 1984 growth in net music revenues despite a weak marketplace caused by worldwide economic problems and the chronic obstacles of home taping and piracy. Strong product from the domestic WEA labels and the emergence of several international artists as worldwide stars enabled WEA International to increase its share of such key markets as the United Kingdom, Germany and Sweden. In addition, WEA Japan, Hong Kong, Australia and New Zealand all experienced record years.

Several of the WCI Record Group's top U.S. performers were equally popular abroad in 1984, including Warner Bros.' Prince, Madonna, ZZ Top, Chaka Khan and Van Halen; Elektra/Asylum's the Cars, Linda Ronstadt, Motley Crue and Womack and Womack; and Atlantic's Honeydrippers, Sister Sledge, Twisted Sister and Yes. Another Atlantic artist, Laura Branigan, had a major international success with her third album *Self Control*, which achieved gold or platinum status in over a dozen countries.

In 1984, major national artists to break through at home and abroad included the United Kingdom's Howard Jones, Strawberry Switchblade and Matt Bianco; Germany's Alphaville; and Canada's Honeymoon Suite. Other key contributors included France Gall in France, Italy's Novecento and Japan's Akina Nakamori.

WEA Manufacturing. The success in 1984 of WEA Manufacturing, the major supplier of the manufacturing needs of the WCI Record Group, was due largely to the outstanding sales achieved by WCI recording artists during the year as well as the company's continued strong relationships with a number of outside clients. In 1984, cassette tape manufacturing capacity expanded by more than 50% to meet the demand that resulted from the WEA labels' combined success and the dramatic increase in consumer desire for prerecorded cassettes. The strong year meant sizeable increases in volume for all configurations as well.

Warner Bros. Music (WBM), WCI's domestic and foreign music publishing operation, reported all-time high revenues and operating income in 1984, surpassing marks set the previous year. This record showing is attributable to the quality of WBM's catalog and the continued strong demand for music in a variety of forms. This demand is being fueled by the recent emergence of a number of innovative new outlets for music including video music, home video and compact discs. A 6% increase in the mechanical royalty rate, which took effect in July, is also partially responsible for the year's gains.

WBM either owns or controls the rights to more than 300,000 musical compositions ranging from standards by George and Ira Gershwin, Cole Porter and Rodgers and Hart to songs by such modern-day stars as Prince, Madonna, Michael Jackson, Cyndi Lauper and Lionel Richie; in 1984, each of the latter five artists had multi-million selling recordings. WBM also controls the rights to the film music of Lucasfilm, Ltd.—producer of the *Star Wars* movies—and Twentieth Century-Fox, as well as songs from such well known Broadway shows as *Dreamgirls*, *My One and Only* and *42nd Street*. In 1984, touring productions of *42nd Street* in the U.S. and abroad helped generate revenues for WBM.

16. Segment Information

Information as to WCI's continuing operations in different industry segments is as follows:

Years ended December 31 (Thousands)	1984	1983	1982
Revenues from unaffiliated customers:			
Filmed entertainment	$1,090,042	$ 848,498	$ 667,610
Recorded music and music publishing	817,575	765,933	752,317
Publishing and related distribution	115,896	108,778	88,848
Total	$2,023,513	$1,723,209	$1,508,775
Operating income:			
Filmed entertainment	$ 150,384	$ 109,317	$ 102,956
Recorded music and music publishing	89,604	60,724	58,656
Publishing and related distribution	15,998	14,273	12,518
Total operating income	255,986	184,314	174,130
Unallocated expenses, net	(186,367)	(217,890)	(161,198)
Income (loss) before income taxes	69,619	(33,576)	12,932
Benefit (provision) for income taxes	(56,500)	22,600	(29,200)
Income (loss) from continuing operations	$ 13,119	$ (10,976)	$ (16,268)

The Recorded Music and Music Publishing division distributes home video cassettes for the Filmed Entertainment division. A change in the allocation of home video revenues and costs between the divisions in 1984 increased the revenues and operating income of the Filmed Entertainment division by $98,567,000 and $6,000,000, respectively, and decreased the revenues and operating income of the Recorded Music and Music Publishing division by corresponding amounts. Revenues from the distribution of the home video cassettes of the Filmed Entertainment division that were recorded by the Recorded Music and Music Publishing division in 1984, 1983 and 1982 amounted to $19,538,000, $100,476,000 and $49,925,000, respectively.

Years ended December 31 (Thousands)	1984	1983	1982
Total assets:			
Filmed entertainment	$ 778,905	$ 814,297	$ 893,201
Recorded music and music publishing	384,227	374,907	384,159
Publishing and related distribution	27,165	27,518	23,070
Net assets of discontinued businesses	231,252	737,169	795,505
Corporate	801,482	790,943	601,934
Total	$2,223,031	$2,744,834	$2,697,869

Corporate assets consist principally of cash, marketable securities, other investments and deferred income taxes.

Years ended December 31 (Thousands)	1984	1983	1982
Capital expenditures:			
Filmed entertainment	$ 6,973	$ 3,366	$ 4,483
Recorded music and music publishing	10,750	10,292	12,006
Publishing and related distribution	1,269	1,568	1,320
Corporate	12,227	23,246	18,955
Total	$ 31,219	$ 38,472	$ 36,764
Depreciation and amortization:			
Filmed entertainment	$ 2,603	$ 2,333	$ 2,809
Recorded music and music publishing	14,126	15,615	15,990
Publishing and related distribution	1,295	888	914
Corporate	4,733	7,086	5,250
Total	$ 22,757	$ 25,922	$ 24,963

Results of Operations

1984:
In 1984 WCI had revenues from continuing operations of $2 billion, income from continuing operations of $13.1 million, or $.12 per share, and a net loss of $586.1 million, or $9.73 per share. Those results compare to revenues from continuing operations of $1.7 billion, a loss from continuing operations of $11 million, or $.17 per share, and a net loss of $417.8 million, or $6.44 per share, in 1983.

The operating results of Atari and sales of its principal assets have resulted in after tax losses of $1 billion during the past two years—$585.2 million in 1984 and $414.7 million in 1983. The remaining operations that were discontinued in 1984 accounted for a combined after tax loss of $18.6 million during the same period—a $26.5 million loss in 1984 and income of $7.9 million in 1983. The 1984 loss includes a $101.6 million gain from the sale of Warner Cosmetics and sizeable reductions in the carrying value of the net assets of Franklin Mint and other non-Atari discontinued operations.

With respect to WCI's core businesses, the Filmed Entertainment division and the Recorded Music and Music Publishing division had exceptionally good years in 1984. Their performance is the major reason why operating income increased to $256 million, compared to $184.3 million in 1983.

Filmed Entertainment revenues increased to $1.1 billion in 1984, an all-time high, compared to $848.5 million in 1983. Operating income increased to $150.4 million, compared to $109.3 million in 1983. Warner Bros. was the motion picture industry's top performer at the box office in 1984 and earned domestic film rentals of $304.7 million, compared to $203.3 million in 1983. Led by *Gremlins*, the studio's top ten theatrical films earned domestic film rentals of $248.6 million in 1984 compared to $180.2 million earned by the top ten films of 1983. Substantial amounts of income were earned in 1984 and 1983 from previously released theatrical films that became available for telecasting and from home video sales, which is indicative of the importance of all markets to the increasing value of the Warner Bros. film library. The television division also achieved record revenues and operating income in 1984, in large part because of the revenues and income recognized when *The Dukes of Hazzard* series became available for syndicated telecast.

Revenues of the Recorded Music and Music Publishing division increased to $817.6 million, an all-time high, compared to $765.9 million in 1983. Operating income increased from $60.7 million in 1983 to $89.6 million in 1984, second only to 1978's record $92.6 million. All domestic companies in this division contributed to this year's improvement, particularly Warner Bros. Records which, led by worldwide sales of almost 11 million copies of Prince's *Purple Rain* album, had the best year in its history. WEA International's results decreased in 1984 due in part to a stronger U.S. dollar and to a change in the allocation between the Filmed Entertainment division and the Recorded Music and Music Publishing division of home video revenues and profits.

Publishing's revenues increased to $115.9 million in 1984, compared to $108.8 million in 1983. Operating income increased to $16 million, compared to $14.3 million in 1983. Warner Books, DC Comics, *Mad Magazine* and Warner Publisher Services each improved over last year.

Corporate general and administrative expenses have been reduced to $57.7 million in 1984, compared to $96 million in 1983. Such expenses declined to $10.5 million in the fourth quarter of 1984 and are expected to continue to decline in 1985. Across-the-board spending and personnel cuts and lower professional fees account for most of the decreases.

WCI's share of the pretax operating results of its investments in broadcast and cable television companies amounted to a loss of $40.8 million in 1984, compared to a loss of $63.8 million in 1983. Warner Amex's 1984 pretax loss amounted to $94 million (WCI's share, after eliminations, was $48.6 million), compared to $150 million in 1983 (WCI's share, $75.0 million). Compared to last year, Warner Amex reduced its operating loss by $60.9 million; realized a $61 million gain on the sale of one-third of MTV Networks Inc. to the public; and had losses of $39.3 million on dispositions of cable systems, compared to gains in 1983 of $19.7 million. In addition to the 1984 loss on disposition, the three metropolitan cable systems that were sold in 1984 and a fourth that is being held for sale in 1985 generated losses of $108.9 million in 1984 and $77.2 million in 1983. Showtime/The Movie Channel, an investment made late in 1983, and BHC, an investment made early in 1984, contributed pretax earnings, which reduced WCI's combined loss on its broadcast and cable operations.

Other income, net, decreased from $56.3 million in 1983

MAGAZINE AND NEWSPAPER ARTICLES

[From the Billboard, Sept. 15, 1984]

CHAINS SEE AMBITIOUS EXPANSION

BOOM IN NEW STORE OPENINGS THROUGH 1985 PREDICTED

(By John Sippel)

LOS ANGELES—Encouraged by an upward record/tape business spiral and the prospects of a continuing home video software surge, industry retail chains expect their most ambitious new store expansion since 1980 over the next 15 months.

In addition to new locations, chain real estate executives like Rich Gonzales of the 154-store Record Bar anticipate thousands of dollars in complete and partial renovations. "We expect to open possibly 15 more stores in malls," he says. "There will also be more home video outlets, like the ones in Norfolk and Jacksonville, N.C. We expect some kind of renovation in 30 existing stores." Gonzales estimates that capital expansion for the Bergman chain will exceed $2 million in 1985.

The Boston-based Strawberries, now at 42 stores, will climb to 50, owner Morris Levy states. "We expect to start to fill in stores in New Jersey before the end of 1984, and the addition of stores in Jersey will continue in 1985," Levy says. " We opened our first home video department within a Strawberries two months ago," he continues. "I expect 10 by the start of 1985. It takes 1,000 feet in a larger store to do it right." Levy, too, sees several million dollars going into store expansion.

Turtles, the 42-store chain recently acquired from Alan Levinson by Clinton Holding, expects to add eight more stores, and is also mulling further acquisition, Levinson reports. Turtles, which recently acquired six Ox stores out of Birmingham, is seeking larger locations, favoring 3,500 to 4,000 square feet over its present 2,500 square foot size. "We need room for more movies, cassettes and accessories," Levinson says.

With his chain currently at 20 stores, John Torrell of Rainbow, San Francisco, is opening Bay Area stores in Concord, Fremont and Dublin before year's end. "I think business will remain good," he says. "We look for three more stores in 1985. We are adding movie rental continually—we have it in four now and see it in maybe 10 by the year's end."

Like a number of his peers, Lee Cohen of Licorice Pizza here is pumped up by the optimism prevalent at the recent VSDA convention. The Jim Greenwood-owned chain has 34 outlets in the southern half of California and is opening at least two more this year.

Cohen says he wants complete home video departments in all stores, with emphasis on CDs, too. Many will have TV monitors displayed prominently.

"We are in the process of upgrading that old burlap look in all Licorice Pizza stores," Cohen comments. He forecasts two or three more openings in 1985.

Mother's Records, Norfok, Va., is testing its first leased department, opening soon in a Winston's Discount store in Tallahassee. "It's only 700 square feet, but we are watching it," Al Bernard states. "We want more cassettes and CD in our product mix. We will stock music videos, but are still wary of heavy movie inventories."

Roy Imber of Elroy Enterprises on Long Island sees as many as four more Record World stores opening by the end of the year, bringing his total to 50 along with 12 leased departments in the area. Imber sees cassettes playing a greater role in monthly album sales, along with CD and blank video tape sales gains.

Noting the presence of many video specialty shops in his vicinity, Imber remains wary of home video departments. He projects five to seven more stores in 1985.

Now operating six stores in the greater Augusta, Ga. area, Robert Allen of Home Folks News & Records there intends to open two more stores this year and a similar number in 1985. "Video will be our top priority" he says. "We are adding it in our first location, with more to come." He is starting out with a 200-title home video inventory.

Record Factory, the 34-store string in the Bay Area, is investigating relocations more than new stores, according to marketing chief Bob Tolifson: "We like to be tops in a market. We want the superior location. We bank a lot on what happens this fall.

"If business remains good, we might even take a chance of going out of state. We'll probably open four more stores and relocate six in 1985."

Believe In Music, the Michigan chain, will open two more outlets this year, bringing its central state total to nine. Russ Stuut and Jim Marcusse there are introducing their first full video department soon and see that trend continuing. They expect to add several more stores in 1985, with one opening already certain next March.

Mary Ann Levitt, who recently moved her base to Sausalito, Calif., is opening no more Record Shops in 1984, but sees as many as four more in her 1985 planning. She envisions no home video entry, however, as she finds mall landlords frowning on rentals.

Kemp Mills, now at 25 stores in the Baltimore-Washington area, may open two more this year and two or three more next year, Darryl Sherman asserts. He wants more room for CD inventory.

John Marmaduke's 135-store Hastings Books & Records out of Amarillo is planning three new stores by the end of the year, and is committed to opening an additional three or four in 1985. According to Marmaduke, the chain's product mix has expanded to encompass more cassettes and video, and existing and future floor plans have been altered to accommodate the product shift.

[From the Billboard, Nov. 10, 1984]

RCA Reports Hike in Earnings

THIRD QUARTER FIGURES

New York—RCA Corp. has declared earnings of $78 million or 74 cents per share for the third quarter ended Sept. 30, based on sales of $2.47 billion. The figures represent a hike of 28.8% in earnings over the same quarter of last year.

Although the company did not make division-by-division breakdowns available, the Consumer Electronics division, which includes RCA Records, was touted as having "record profits." Without offering figures, the firm also lauded the performances of its NBC, Hertz and Communications divisions.

For the first nine months of 1984, RCA's earnings rose more than 56% to $238.2 million or $2.27 per share, as compared with $152.1 million or $1.23 per share a year ago. Sales for the first nine months increased to $7.32 billion, as compared with $6.49 billion last year. During the first nine months of 1984, RCA has enjoyed a $175 million special provision, taken in the first quarter, for restructing its VideoDisc operation, as well as a $75.7 million benefit from the cumulative effect of a change in the method of accounting for investment tax credits.

[From the Billboard, Feb. 23, 1985]

CBS 1984 Profits Up 13%

FOURTH QUARTER LESS THAN THRILLING

(By Irv Lichtman)

New York—The CBS/Records Group survived a 43% drop in 1984 fourth quarter profits to register a 13% rise for all of 1984.

CBS Inc., reporting results for the three months ending Dec. 31 and for the entire year, said last week that the fourth quarter drop resulted mainly from a "difficult comparison" with 1983, when the company was riding on the crest of Michael Jackson's "Thriller" album, which has gone on to sell 35 million copies globally.

In dollars, the fourth quarter results amounted to profits of $19.4 million, compared to $33.8 million a year before. For all of 1984, profits climbed 13% to $123.5 million, compared to $109.4 in all of 1983.

Sales for the fourth quarter at the division—which includes both the domestic and international CBS labels, Columbia House, the direct-mail unit, and CBS Songs, the music publisher—declined 4% to $311.8 million from $326.2 million. Sales for the year climbed 9% to $1,265.1 billion from $1,158.8 billion.

According to the CBS Inc. report, both the domestic label and Columbia House sparked gains for the year. The strengthening dollar adversely impacted on profits at the international label, although revenues improved "modestly." Cited was a profit decline at CBS Songs, reflecting a non-recurring gain in 1983 on the sale of its Big 3 Music print division to Columbia Pictures Publications.

[From the Billboard, Mar. 2, 1985]

FEBRUARY SALES HAVE STRONG HEARTBEAT

VALENTINE'S-TO-PRESIDENT'S DAY SPREE

(This story prepared by Earl Paige in Los Angeles and Fred Goodman in New York)

NEW YORK—The five-day shopping period between Valentine's and Presidents' Days is being termed a high point in an unusually strong February by record and tape retailers.

"We experienced an increase over the weekend of between 25% and 40%, depending on location," says Jerry Dolan, retail systems supervisor for the North Canton, Ohio-based Camelot Music. Although the 167-store chain elected to concentrate its promotional efforts on the Grammys rather than the shoppers' holiday (Billboard, Feb. 23), Dolan attributes the hike to "added shoppers in the malls."

In Detroit, sales were strong for the 16-store Harmony House chain, according to buyer Lloyd Welch, although he, like others, doesn't yet have hard figures to back that statement up. "We've had a lot of snow for a week and a half here, but we're up," he says, adding that Valentine's Day helped, with all stores running product at $6.99.

The 136 stores in the Amarillo-based Hastings chain saw a comparable sales hike of 11%, according to marketing vice president Bruce Shortz. He indicates that Presidents' Day activity was good enough to "catch some of our stores understaffed." Shortz merchandised towards Valentine's Day with a "heartbeats" Valentine's campaign using blue and burgundy for print and in-store material. The chain went $2 off on a wide-ranging group of 24 titles.

The 36 mid-Atlantic Kemp Mills have been having "a great February," according to co-owner Howard Applebaum, who terms Presidents' Day "tremendous," although he credits the rise in sales to the chain's discount pricing policy.

The Long Island-based Record World chain didn't run anything special for Valentine's Day, according to merchandising director Tom Pettit, and Presidents' Day was incorporated into the chain's normal advertising. Yet Pettit also terms February business "very good" for the 60-store outfit.

One retailer that aggressively pursued Valentine's Day was the Missouri-based Streetside chain. Buyer Tom Lunt says the eight-store web's four-day "Streetside Loves You" campaign produced the best sales response of any campaign since 1981. "We just did spectacular," he says, adding that the chain's markets, which include St. Louis, Kansas City and Columbia, could have benefitted from a "cumulative effect, since there were a lot of other accounts running sales."

Although Valentine's Day figures have yet to be totaled, Tower Records' Stan Goman says the chain has been chalking up record figures of late. Goman, who is division manager at Sacramento, says the chain was up 31% for the first two weeks of February, with video "incredible, up 108%."

Tower ran no Valentine's Day promotion per se because it was holding "CBS month" as the largest basic promotion. Renovations at the lower New York annex also produced a massive clearance sale, contributing to that outlet's strengthened showing.

[From the Billboard, Mar. 2, 1985]

MUSIC BRIGHTENS PICTURE FOR MCA INC.

1984 REVENUES UP, INCOME DOWN

(By Sam Sutherland)

LOS ANGELES—The continuing turnaround for the MCA Records & Music Group and the burgeoning home video market provided bright spots in an otherwise disappointing fiscal 1984 performance for MCA Inc. Although the entertainment conglomerate reported the highest revenues in its history, both operating income and net income fell below comparable figures for 1983.

Revenues were $1,651,242,000, as compared to $1,584,539,000 for 1983. Operating income for the year ended Dec. 31 was $96,594,000, and reported net income was $94,937,000 or $1.96 per share. Those statistics compare with 1983's operating income of $184,698,000 and net income of $147,160,000 or $3.06 per share.

MCA's theatrical motion picture operations were cited as the primary cause for the reduced earnings, while the MCA Records & Music Group rebounded from 1983's losses in operating income of $8,839,000. Revenues for the division reached $255,930,000 as compared to $188,104,000 a year earlier; included in those tallies are fees for domestic home video distribution.

Home video and pay television also fared well. Although no net or operating income figures were provided, revenues rose to $160,296,000 during 1984, comparable to $118,944,000.

Final quarter figures showed the MCA Records & Music Group posting revenues of $76,753,000 and an operating income of $3,769,000, compared to fourth quarter '83 figures of $75,034,000 and $760,000 respectively.

In releasing the data, MCA also cited the effects of home video distribution income and Motown product distribution as enhancing that division's performance. During 1984, MCA also benefited from a lower effective income tax rate, owing to a lower average level of investments and lower investment income.

Overall fourth quarter revenues were $496,951,000 comparable to $395,424,000 during 1983, while operating income was $21,065,000 as compared to $32,079,000 a year earlier. Net income was $18,584,000 or 39 cents per share, compared to $24,890,000 or 52 cents per share in 1983.

[From the Billboard, Mar. 16, 1985]

WARNER BROS. MUSIC: "BIGGEST YEAR EVER"

KAYE POINTS TO MULTIMEDIA THRUST

(By Sam Sutherland)

LOS ANGELES.—Expansion through major catalog acquisitions, a renewed multimedia thrust tying music to films and TV, and operational streamlining have culminated in Warner Bros. Music's "biggest year ever," according to chairman Chuck Kaye. Kaye, who assumed the top slot at the Warner Communications division in June, 1981, claims a bullish 1984 bears the fruit of that strategic blueprint, which has also emphasized an aggressive move into country music and new overseas acquisitions.

The veteran publisher, who helmed both Almo/Irving Music and a subsequent joint venture firm with David Geffen, Geffen/Kaye, contends his emphasis on catalog purchases and emerging multi-media opportunities was already in place when he sold Geffen/Kaye to Warner Communications Inc. and stepped into the Warner Bros. Music post.

"I had a long talk with David Horowit," he recalls, referring to the former top WCI executive, now with MTV Networks. "I said, 'David, it's a different era now. When I was with A&M, you could really develop artists as a base for growth.' " For the '80s, however, Kaye says he was convinced that new technologies would play a central role.

In fact, one of his first priorities was to modernize the division's internal operations by setting up a new computer system to streamline royalty payments and generally improve data management throughout the company.

More visible progress came with Kaye's drive to rebuild Warner Bros. Music's ties to the motion picture industry, starting with its sister movie division. "The first company I was after in terms of acquisitions was 20th Century-Fox," he adds, noting that the subsequent Fox deal brought with it the "Star Wars" scores of John Williams, Johnny Mercer's catalog and myriad film music copyrights.

"I felt that with cable and home video now looming, and all those reuse fees growing, it was an important move," he notes. He's quick to stress, however, that the ongoing emphasis on film, TV and video opportunities via ties to Fox and Warner Bros. Pictures "isn't intended to take away from what we're doing with pop, rock, country and black music."

Country, too, spurred an acquisition, in this case the joint-ventured House Of Gold operation helmed by Bob Montgomery. "We wanted to acquire a good contemporary pop/country operation, and we wanted to have a string of good producers involved, so we wouldn't have to go outside to place all our material," says Kaye, who notes House Of Gold's steady production output via Montgomery and Blake Mevis, both well established Music Row producers.

A second joint venture between producer Jim Ed Norman and Warner Bros. Records has also added lustre to the music division's successful "invasion" of the country music capital.

As for the company's fortunes abroad. Kaye faced a major obstacle when Rob Dickens left the London operation to accept a top post with WEA International. "I didn't want to stop him, so I let them have him and kept him on as a director," Kaye notes. "Rob has since gone on to sign acts that we've successfully wooed for publishing."

To further buttress its international roster, which has represented a major force in Warner Bros. Music's earnings since the late '60s, Kaye purchased the publishing catalog run by Johnny Sterling, noteworthy for the copyrights of Phil Collins and Culture Club songwriter Phil Pickett. Other recent U.K. acquisitions include Astec Camers, New Order, Bananarama, Wang Chung, Modern English, the Human League, Madness, Howard Jones, Whitesnake, John Wetton, Trevor Rabin and the Clash.

U.S. songwriters signed for overseas representation include Lionel Richie, Bob Dylan and Neil Diamond, while domestic hits for Prince, Madonna and Talking Heads have capped income from American writers pacted to Warner Bros.

[From the Billboard, Mar. 23, 1985]

1984 A PEAK YEAR FOR RECORDINGS

(By I.S. Horowitz)

NEW YORK—Net shipments of recordings by U.S. manufacturers approached $4.5 billion at suggested retail last year, a new high for the industry.

The 1984 estimate by CBS researchers, disclosed to a group of financial analysts last week (separate story, page 78), pegged the value of shipments at $4.464 billion, some 17% over the 1983 tally of $3.815 billion, and 8% more than the $4.132 billion racked up in 1978, the industry's previous peak year.

Shipment figures assembled by the Recording Industry Assn. of America (RIAA) will not be available until the National Assn. of Recording Merchandisers (NARM) convention at month's end, following a meeting of the RIAA market research committee. In past years, however, the CBS estimates have been accurate harbingers of the RIAA statistics.

CBS also documented for the analysts the vigor of the prerecorded videocassette market by estimating unit shipments in 1984 at 22 million, up 100% over the prior year. In 1985, the company predicted, unit shipments will rise another 60% to 35 million. Latter figure tops by two million an earlier prediction by the Electronic Industries Assn.

Computer software shipments in 1984, said CBS, were valued at $380 million, an increase of 52% over 1983's $250 million. The predicted value of computer software shipments in 1985 was given as $448 million, up 18% over 1984.

While the CBS statistics on audio recordings furnished no breakdown of the various configurations, it's believed that cassettes have continued to grab off an increasing market share, as LPs decline. When the RIAA figures are released, they are also expected to show a dramatic rise in shipments of Compact Discs, thought by some to have reached about 4.2 million last year.

Significantly, the CBS estimates for 1984 extended the prediction of an industry turnaround indicated by half-year figures released last October by the RIAA. The gain for that period over the same period a year earlier, was 15% in dollars and 17% in units, the RIAA said.

Further support comes from NARM, where one source puts the increase in sale of a representative sample of member stores at 23% from September through the end of the year. Figures the association released earlier showed sales up 17% for the first seven months of the year. However, those tallies also included sales of blank tape and accessories.

In international markets served by CBS, industry volume for recordings was put at $3.770 billion in 1984, 3% over the 1983 total of $3.661 billion. The prediction for 1985 is $3.790 billion, a marginal gain of 0.5%

U.S. direct mail sales, said CBS, were estimated at $475 million for 1984, up 8.2% over 1983 when the figure was $439 million. In 1985, says CBS, direct mail sales will rise another 5.5% to $501 million.

[From the Billboard, May 4, 1985]

WCI RECORD GROUP SOARS

BUT OVERALL NET INCOME DECLINES

NEW YORK—Record quarterly revenues for its recording group division and strong filmed entertainment division business provide highlights in Warner Communications' fiscal report for the first quarter of 1985. But despite those bright spots, which contributed to gains in both overall revenues and income from continuing WCI operations, net income declined.

The WCI Record Group posted its highest first quarter revenues in the corporation's history, with revenues of $225 million, a 26% increase over first quarter '84. Operating income rose 42% for the quarter just ended, reported as $30.2 million by WCI Warner Bros. and Atlantic Records were cited as contributing strong sales, as were three WEA-distributed albums that reached the top rung on Billboard's pop album chart: Phil Collins' "No Jacket Required" (Atlantic), John Fogerty's "Centerfield" (Warner Bros.) and Madonna's "Like a Virgin" (Sire).

The report also claims substantial increases for the quarter in both revenues and operating income by WEA International, although no specific figures are broken out of the overall recording sector figures; overseas, Collins and Foreigner were cited as the most notable of various WEA acts contributing to the gains.

Continued growth for WCI's home video business was also noted, although precise revenue and income figures for Warner Home Video were not supplied. Overall, the filmed entertainment division, of which the home video arm is a part, increased its operating income by a marginal $1.1 million, rising to $40.6 million for the quarter just ended.

Operating losses for WCI's broadcast and cable operations also declined sharply, dropping from $16.3 million during the first quarter of 1984 to $4.4 million for the quarter just ended. Cost savings, reduced interest expense and improved operating results for the Warner-Amex division are noted.

[From the Billboard, May 11, 1985]

APRIL SHOWER

TWICE AS MANY PLATINUM ALBUMS AS '84

(By Paul Grein)

LOS ANGELES—The Recording Industry Assn. of America (RIAA) certified eight platinum albums in April, twice as many as in April, 1984. It was the fourth straight month that platinum certifications outstripped 1984 monthly totals. For the year to date, the RIAA has awarded 28 platinum albums, compared to just 17 by this point in '83 and '84.

Leading the list of platinum albums was Alabama's "40 Hour Week," the group's sixth album in a row to top the million sales mark. Also certified platinum in April was Eddie Murphy's "Comedian," first released in November, 1983. It's the first comedy album to top the million sales plateau since Steve Martin's "A Wild And Crazy Guy" in 1978.

Deep Purple's "Perfect Strangers" also went platinum in April, capping a tour-boosted comeback. It's the group's first platinum album, a reflection of the fact that the group's biggest albums—"Machine Head" and "Made In Japan"—were issued prior to the inception of platinum awards in 1976.

USA For Africa's album "We Are The World" went platinum and double platinum in April, while the "We Are The World" single was certified for selling four million units. It's the first single to earn multi-platinum certification since the new award was created by the RIAA last December.

Daryl Hall & John Oates were also inducted into the multi-platinum awards program in Arpil. Their last three album releases—"H_2O," "Rock 'N Soul" and "Big Bam Boom"—were all certified double platinum.

And Phil Collins earned his second platinum album in as many months with "No Jacket Required." Collins' 1982 release "Hello, I Must Be Going!" topped the million mark in March.

Don Henley's second solo album, "Building The Perfect Beast," also went platinum in April. It's the first platinum solo album by a former member of the Eagles. Henley's 1982 debut album, "I Can't Stand Still," went gold.

David Lee Roth's solo debut, "Crazy From The Heat," went gold in April. With Van Halen, Roth has collected six consecutive platinum albums, with combined certified sales in excess of 18 million.

The month's top album award went to Madonna's "Like A Virgin," which was certified quadruple platinum; Madonna's self-titled debut album was certified double platinum last December.

Here's the complete list of April certifications:

MULTI-PLATINUM ALBUMS

Madonna's "Like A Virgin," Sire/Warner Bros. Four million.
Daryl Hall & John Oates' "Big Bam Boom," RCA. Two million.
Daryl Hall & John Oates' "H_2O," RCA. Two million.
Daryl Hall & John Oates' "Rock 'N Soul," RCA. Two million.
USA For Africa's "We Are The World," Columbia. Two million.

PLATINUM ALBUMS

Alabama's "40 Hour Week," RCA. Their sixth.
Phil Collins' "No Jacket Required," Atlantic. His second.
Deep Purple's "Perfect Strangers," Mercury. Their first.
Don Henley's "Building The Perfect Beast," Geffen. His first.
Eddie Murphy's "Comedian," Columbia. His first.
USA For Africa's "We Are The World," Columbia.
Various Artists, "Beverly Hills Cop" soundtrack, MCA.

GOLD ALBUMS

Alabama's "40 Hour Week," Alabama, RCA. Their sixth.
Phil Collins' "No Jacket Required," Atlantic. His third.
Teena Marie's "Star Child," Epic. Her second.
George Strait's "Does Ft. Worth Ever Cross Your Mind," MCA. His second.
George Winston's "Autumn," Windham Hill/A&M. His second.
Autograph's "Sign In Please," RCA. Their first.
"The Firm," Atlantic. Their first.
The Judds' "Why Not Me?," RCA/Curb. Their first.
David Lee Roth's "Crazy From The Heat," Warner Bros. His first.
USA For Africa's "We Are The World," Columbia.
Various Artists, "Vision Quest" soundtrack, Geffen.

MULTI-PLATINUM SINGLES

USA For Africa's "We Are The World," Columbia. Four million.

PLATINUM SINGLES

USA For Africa's "We Are The World," Columbia.

GOLD SINGLES

USA For Africa's "We Are The World," Columbia.

[From the Billboard, Nov. 2, 1985]

WEA REPORTS RECORD QUARTER

INTERNATIONAL SALES AID SHOWING

(By Steven Dupler)

NEW YORK—Warner Communications Inc. reports record third quarter earnings for its recorded music and music publishing division.

Operating income for the division was up 4%, from $22.7 million in 1984's third quarter to $23.6 million in 1985, a new divisional high. At the same time, the division's earnings for the nine-month fiscal period ending Sept. 30 were $78 million, representing an increase of 36% more than the same period in 1984.

The recorded music division's total operating revenues for the third quarter, however, remained basically unchanged, dropping slightly from $209,284,000 last year to

$209,280,000 this year. Still, for the first nine months of 1985, operating revenues increased considerably from $566,286,000 in 1984 to $642,157,000 in 1985.

WCI chairman and chief executive officer Steve Ross attributes much of the music division's success in the quarter and the first nine months of the year to contributions made by acts such as Madonna, Phil Collins, Motley Crue, Dire Straits and Ratt, as well as "very strong international results."

WCI also saw dramatic gains in its broadcast and cable communications division. Third quarter operating income increased more than 200%, from a 1984 loss of $6.2 million to a 1985 figure of $6.4 million. For the nine-month period, the broadcast and cable division's earnings were $2.4 million, a substantial increase from the loss of $35.8 million reported for the first nine months of 1984.

Ross cites WCI's sale of its 31% stake in Showtime/The Movie Channel as well as Warner Amex's two-thirds interest in MTV Networks and its 19% interest in Showtime/The Movie Channel to Viacom International as being primarily responsible for the division's strong performance. WCI receives $500 million in cash, plus additional warrants to acquire as much as 2.25 million shares of Viacom's common stock as part of the agreement.

WCI's film division also reports a record third quarter and nine-month period. Operating revenues for the quarter rose to $319,656,000 from $302,284,000; revenues for the nine-month period increased from $566,286,000 to $642,157,000. Operating income of $54.9 million for the quarter was up 4%, while income for the first nine months rose 7% percent, exceeding last year's previous high, to $131.8 million.

WCI's overall third quarter income was $34.06 million, or $.50 per share, representing a nearly three-fold increase over the same period last year.

[From the Billboard, Nov. 30, 1985]

MCA's Growth Ahead of Schedule

CHART FIGURES OFFER EVIDENCE OF DRAMATIC TURNAROUND

(By Sam Sutherland)

Los Angeles—A bullish growth curve in both revenues and profits plus a substantial increase in share of chart action underscore MCA Records Group's revitalized posture in recent quarters.

With recent weeks marking what is believed to be the company's broadest album chart profile to date, senior MCA executives are basking in fresh evidence of what may be the most dramatic turnaround for a major label this decade.

That's the upbeat stance taken by the senior management team assembled since Irving Azoff's arrival some 30 months ago to assume the top slot in a then beleaguered music division, still limping back into black ink after significant net losses. Azoff's team now points to a number of heartening indicators that the "new" MCA is ahead of schedule in its timetable for growth:

Recent quarters have witnessed the division's slice of parent MCA corporate revenues and net income swelling to record levels. For the first nine months of 1985, the group's gross revenues rose to $204,032,000 from $179,177,000 a year ago, while operating income was pegged at $13,456,000, comparable to just $5,070,000 for the same period in 1984. Those figures also compare dramatically to full-year totals from 1982, the last year prior to Azoff's ascendance, when operating income was $7,878,000 on revenues of $49,745,000.

Analysis of Billboard chart activity in recent weeks caps MCA's evident gains in black, country and pop singles action, with the division's growth past 20 of the top 200 albums—claimed as an all-time high by MCA staff— to 23 albums from MCA and its distributed labels, including Motown and IRS, on this week's album listings.

Share of chart action against competitive labels has meanwhile increased to an estimated 13.1% during the first six months of this year, including Motown's substantial collective share of 5.7% for its labels but excluding IRS. That conservative figure places the MCA Group firmly in fourth place after WEA, CBS and the RCA/Arista/A&M fold in terms of distribution entities. In 1982 MCA was the seventh-ranked distribution major.

Those figures prove even more impressive in light of even lower revenues and operating income tallies reported during the first quarter of 1983, just prior to Azoff's appointment as president of the division. Since then, explains Myron Roth, executive vice president for the group, Azoff and his realigned senior managment team have literally rebuilt the company through extensive re-staffing in key posts, an overhaul in the division's structure, aggressive expansion in its distribution activity via client lines, and an extensive revamping of MCA's own artist roster.

"What Irving and I thought would take us five years to accomplish, we've achieved in just two years," exults Roth, who left his post as CBS Records' senior West Coast operational chief to join Azoff at MCA. "When you consider that we've accomplished this without a major flow of international product sales, I think that's impressive."

Roth's own appointment was just one of a flurry of additons to the MCA team during a substantial overhaul of the company's structure and key staff. Arista promotion chief Richard Palmese was enlisted to helm both promotion and marketing; A&M black promotion chief Jheryl Busby was tapped to oversee the entire black music operation for the label; a trio of new, younger A.&R. executives was installed to revitalize signings; and similar changes were made at various middle management positions.

Meanwhile, Roth recounts, the need to revamp MCA's distribution business, then conceded to be a red ink factor in the group's overall performances, was pegged to the new team's most prominent appointment from within: the installation of John Burns as head of MCA Distributing. "The other major decision along those lines was to not run distribution as a separate company, as it had been before, but as part of the overall operation," observes Roth.

"Increasing the [distribution] volume to attain profitability was a major part of the decision to distribute Motown," Roth continues, "but there were other factors involved in that decision as well."

Increasing MCA's profile in black music, a field in which Roth maintains the company was "completely dormant" during the early '80s, was also a prime goal in the Motown negotiations. Motown president Jay Lasker agrees that his label's swing to MCA from its long history as an independently distributed line brought MCA instant credibility, but Lasker stresses that the benfits from the association have been far from one-sided.

"We know we've been very instrumental, especially in the beginning, in helping MCA Distribution become profitable," explains Lasker. "The point is, though, that here at Motown, we've never said, 'Look what we've done for you,' and MCA has never said that to us.

"It's been a mutual gain. The relationship has far exceeded what I expected in terms of being as good for us as it has been. I couldn't ask for a better relationship."

Roth says the courtship of IRS likewise centered on another idiom considered weak in the MCA fold, alternative rock and pop: "We saw [IRS] as an educational process for us. We already had Oingo Boingo and were developing several English and Australian acts. We needed to learn how to handle that market more effectively."

Country dictated a similar move, although the need for a realignment was less obvious. Roth notes that MCA's Nashville profile was being orchestrated by an acknowledged country veteran, Jim Foglesong, yet Azoff elected to bring in Jimmy Bowen, associated with a younger generation of country and country/pop stylists, to shift direction.

Also given priority: investment in new artists, rather than major superstars, to build a core for pop and rock market growth, as well as stepped-up coordination of soundtrack packages to exploit cross-marketing options, a priority that has since paid off handsomely with the albums from "Beverly Hills Cop," "Back To The Future," "Weird Sciences" and, most recently, "Miami Vice."

Ironically, MCA had long had a busy schedule of soundtrack releases yet only periodically reaped major chart successes from that area during the late '70s. "It was different before, in that the label was being fed product from whatever films Universal had," Roth says, "The interesting thing here is the conscious effort we've made to use these soundtracks to really break artist careers.

"Putting Patti Labelle into 'Beverly Hill Cop' is a good example, and putting Glenn Frey into both 'Cop' and 'Miami Vice' is an even better one: His second album and first for us was essentially over when those soundtrack exposures began to rekindle his sales."

Current priorities find MCA adding jazz to its palette, reactivating old catalogs and adding both domestic and imported new product through it new MCA Jazz division under Ricky Shultz; mounting a major quality control drive that has already led to an extensive upgrading of equipment and procedures for MCA's tape product, and is now being extended to its LP pressing floor; a review of the classical market with an eye toward increasing presence there, and a recent swing into more aggressive special products licensing and sales.

"We're going across the board," Roth says of the eventual talent focus in what he projects will soon be a truly full-line operation in terms of both catalog and current releases. That's a long distance from the severe roster shakeout that was the first order of business in 1983, leading to walking papers for 41 of the 46 acts on the MCA roster when Azoff came aboard.

[From Fortune, Apr. 1, 1985]

A YEAR FOR RECORDS

A comeback award for Sixties rocker Tina Turner at this year's Grammys could easily have gone to the whole record industry. It had finally climbed out of the pit of a four-year depression that introduced a novel word, austerity, into its upbeat vocabulary. Record and tape sales by manufacturers climbed 15% to $1.93 billion in the first six months of 1984, according to the Record Industry Association of America, and for the full year could top the all-time high of $4.1 billion set in 1978.

Experts credit the record industry's comeback to the general economic recovery, the role of cable music channel MTV, and the serendipitous emergence of hot artists. CBS's record group reported profits of *$123.5 million in 1984*, up 13% over 1983, on sales of *$1.27 billion.* The CBS lineup features some of the biggest movers of plastic: Michael Jackson (over *20 million copies of Thriller* in the U.S., an estimated 18 million overseas); Bruce Springsteen (5.7 million copies of *Born in the U.S.A.*); and Cyndi Lauper (4.4 million of *She's so Unusual*). Troubled Warner Communications found relief in the sale of ten million copies of Prince's *Purple Rain.* One industry analyst worries that pressures for more giant hits will squeeze out artists with smaller audiences. "Either make it and make it big, or you don't make it at all," says Jerry Shulman, marketing development vice president at CBS Records.

[From the New York Times, Nov. 3, 1985]

A NEW ACT TAKES OVER AT POLYGRAM

(By Fredric Dannen)

At Polygram Records Inc., there are 33½ revolutions per minute. At least, that is how it has looked in the last few years. Polygram has redrawn its organization chart countless times. It has been in and out of myriad new ventures. It has tried in vain to merge with other record companies. And in the process, it has marched presidents in and out its doors. "At Polygram," said one former employee, "by the time you learn to pronounce their names, they're gone."

The company has gone through agencies trying to follow its own act. One of the six largest record companies in the United States, Polygram, the American arm of a worldwide complex of record companies owned by Dutch electronics giant N. V. Philips, once seemed earmarked for stardom. In 1978 it broke industry sales records with the soundtrack albums of "Saturday Night Fever" and "Grease," and hopes ran high throughout Philips that its American subsidiary was on the way to becoming the industry's pacesetter.

But Polygram has been more a profit drain than a star. Between 1979 and 1984 it lost a total of more than $220 million. Its big and costly distribution system has hardly been justified by the paltry number of hit albums it has spewed forth. In fact, industry wags have had a field day mocking Polygram's lack of hits. ("What's the difference between Polygram and the Titanic?" "At least the Titanic went down with a good band.")

This year, at last, the gloom is lifting at Polygram. After a series of cost cutting measures and a surprise burst of pop hits—notably Tears for Fears's smash LP "Songs from the Big Chair" and John Cougar Mellencamp's "Scarecrow"—the company moved back into the black. But Guenter Hensler, the 46-year-old classical music buff who had been heading Polygram since 1941, has had no chance to revel in the restored profitability. On Oct. 21 he was replaced by M. Richard Asher, 52—making Mr. Asher the third man to serve as Polygram's president and chief executive officer since 1983. Mr. Asher's task, company insiders say, is to lure enough pop stars to the Polygram labels to make hit albums the rule, not the exception.

The move stunned Polygram executives, Mr. Hensler, who will resume his old job as head of Polygram's Classics unit, says he "didn't believe it would happen until it did." And Jan Timmer, head of London-based Polygram International, Polygram Records's parent company, and the man who engineered the executive suite shake-up, acknowledges that Mr. Hensler had "proved he could turn the company around."

What he had not proved is that he could attract the types of big-selling recording artists that gravitate to CBS Records and Warner Communications Inc., the industry leaders. Mr. Asher, a 17-year veteran of CBS Records and fresh from a one-year stint with Warner, may have the prestige and experience to do so. And his ascendancy to Polygram's top spot signals that N. V. Philips has not abandoned its dream of making Polygram a heavyweight in the United States market for pop music.

It is a crucial market. Americans buy nearly half the world's records and tapes. Rock music and other pop styles account for more than 90 percent of the $4.5 billion in recordings sold in the United States each year. Although Polygram commands about half the American market for classical records and tapes—its labels include the prestigious Philips, London and Deutsche Grammophon—its share of the pop market sits at a meager 5 percent.

"I don't have the illusion that our market share can grow further in classical music," Mr. Timmer said. "If you want to be an internationally successful record company you must have a certain share of the U.S. pop market, at least 10 to 12 percent. I think we can achieve that in three years' time."

That is a tall order. Polygram could improve its chances by making United States successes of more of the European artists who record for its overseas labels. That would play to Mr. Asher's strengths. At CBS, he brought American star status to Spanish singer Julio Iglesias and to the Australian band. Men at Work.

Mr. Asher has a far better track record for getting along well with artists than with colleagues. An ex-lawyer with a reputation as a tough taskmaster, the gravel-voiced, balding Mr. Asher stands in sharp contrast to the softspoken Mr. Hensler.

Mr. Asher, a native New Yorker who bears a slight resemblance to Alexander Haig, rubbed a lot of people the wrong way at CBS. Walter Yetnikoff, the record group's powerful president, fired him in 1983, citing a clash of personalities.

Mr. Asher scoffs at fears that his arrival will mean bloodletting at Polygram. "I've been in a lot of new situations, and I didn't walk into any of them like Attila the Hun," he said. "I don't intend to do so here, either."

Nonetheless, Mr. Asher probably will shake things up at Polygram a bit by hiring former colleagues. Mr. Timmer has already set precedent for raiding CBS for executives: In addition to Mr. Asher, both Alain Levy and Maurice Oberstein, the heads of Polygram's French and British units, respectively, are CBS alumni.

At present, two key positions at Polygram are vacant: general manager and head of A.&R. (artists and repertoire), the person who signs new acts. "I expect I'll have a tendency to seek out people I know," Mr. Asher said. "Of course, I don't want to overlook anyone within the organization."

His methods and bluntness have won him admiration from some of his colleagues. "Dick Asher is a tough man, but I cannot say anything bad about him," said Fred C. Haayen, former head of Polydor, one of Polygram's pop labels, and now president of Lefrak/21 Entertainment Group. "I think he's one of the strongest record executives in the business."

Philips does not divulge much financial information about the closely held Polygram. But a legal brief filed in 1984, when Polygram tried to merge with Warner, stated that the company lost nearly $300 million before taxes since it entered the United States market in 1969 and that two-thirds of the deficit had occurred between 1979 and 1982. Polygram lost $6 million in 1983 despite two huge hits: the soundtrack recording of "Flashdance," and "Pyromania," an album by heavy-metal rock band Def Leppard. At the time the brief was filed Polygram predicted it would finish 1984 about $15 million in the red.

Polygram's strategic importance to Philips goes beyond profit considerations. Philips is Europe's biggest manufacturer of stereo equipment, and one of the inventors of the compact disk. Polygram's release of music on compact disks has helped the new technology take off. "The introduction of the compact disk would hardly have been possible to Philips without Polygram's support," said Mr. Timmer.

And Polygram has, at last, turned profitable. Mr. Timmer agreed with estimates that the worldwide group should earn about $30 million this year on consolidated sales of $750 million. He added that Polygram Records, the American arm, would contribute 25 percent of the gross, albeit only 10 percent of the profit.

Profitable record companies are few and far between of late. The only record companies with nationwide distribution systems are Polygram, units of RCA, MAC and Britain's Thorn EMI, and CBS and Warner. Of the list, only the last two are "really profitable," said Mark Riely, an entertainment analyst at F. Eberstadt & Company. They together commanded 43 percent of the United States market in 1983, the last year for which figures are available.

Warner and CBS were the only record companies with enough volume to justify national distribution systems, Mr. Riely said. Warner's distribution costs last year, for example, were 8.8 percent of the net sales; Polygram's were 15.87 precent.

Merger seemed the best answer to Polygram's woes. In 1983 Polygram Records had a merger agreement with Warner that would have enabled Polygram to junk its network of warehouses and branch sales offices. Warner would have gotten Polygram's ties to Europe and strength in classics. But the Federal Trade Commission blocked the merger last year, arguing the record retailers would become too dependent on one supplier. Said William E. Willis of the law firm of Sullivan & Cromwell, Polygram's outside counsel, "The F.T.C. wants six major distributors."

Polygram has not given up on the merger idea. It has held talks with MCA and is believed to have approached all the other majors except CBS. Polygram also discussed a merger with non-distributors, notably a consortium led by Alan J. Hirschfield, former head of the 20th Century-Fox Film Corporation. Those talks stalled last June, but Philips is likely to keep searching for someone to buy into Polygram. The Dutch company's original 50-50 partner in the record venture, Siemens A.G. of West Germany, unloaded all but 10 percent of its Polygram equity on Philips last February, adding more impetus to the search for a new partner. Mr. Timmer, however, said. "We're not talking with anyone at the moment."

Meanwhile, Polygram has slashed overhead. This year, Mr. Hensler shut warehouses in California and New Jersey, so that all shipments to retailers are now being made from one huge automated record depot in Indianapolis. He also reduced the number of regional sales offices from 13 to 9 and dismissed about 30 middle-managers.

Might Polygram withdraw from United States distribution altogether, and rely on independent distributors? "Withdraw has a negative connotation," Mr. Timmer said. "But if a reasonable alliance could be made with somebody else in the area of distribution, we would consider it."

Signing hot new performers to cut records remains crucial to Polygram's future. Mr. Hensler had some winners—but not enough. True, Polygram Records latched on to singer-songwriter John Cougar Mellencamp when he was still a virtual unknown, and has introduced some urban black comic acts. But Polygram U.K. has done a far more impressive job of cultivating new acts—Tears for Fears, ABC and Godley & Creme, to name just music. And some of Polygram International's European acts had balked at allowing the company's American arm to distribute their records in the states. Many felt they could get a better deal with CBS or other record companies.

"I often found it difficult to attract artists to be part of our U.S. operations," said Aart Dalhuisen, an A.&.R. executive at Polygram International. "Over the years," added Ron Alexenberg, president of RAA Productions, a company that manages musicians, "Polygram Records has not been at the forefront of breaking new acts."

That goal eluded Mr. Hensler's predecessors as well. "That's why I left," said David A. Braun, an entertainment lawyer at the Los Angeles firm of Wyman, Bautzer, Kuchel & Silbert, who served one year as Polygram's president just prior to Mr. Hensler. "What great artist will sign with Polygram when they can go to CBS or Warner?"

The answer, Mr. Timmer and other Polygram executives clearly hope, is the artist familiar with Mr. Asher's reputation. "I just happen to be an American who has had success with and great respect for international artists," he said of himself. "Think about what it takes to be an artist, to get out on stage, open your viscera and expose it to the world. If you're going to make a living and put bread on your table from the efforts of these people, the least you can do is give it the best you've got."

Industry veterans wonder whether Mr. Asher is not, in fact, being counted on to steal some CBS recording artists. Polygram had that very ploy in mind when it hired Mr. Braun. As an entertainment lawyer, Mr. Braun had represented CBS stars such as Michael Jackson, Barbra Streisand, Bob Dylan and Neil Diamond. Not one defected to Polygram.

"They hired me to tap into the mainstream, and of course it didn't work," Mr. Braun recalled. "The Europeans never understood that the key to building a class record company in the U.S. is to develop artists, not buy them."

"I'm not big for signing superstars," Mr. Asher said. "When you sign artists at the top of the game, you get into a bidding war. There isn't much upside potential in that."

Indeed, royalty rates for some big names are so high—20 percent or more of the list price of each album—that their records must sell in the millions to break even. A far better approach, Mr. Asher said, is to find talented "baby" acts and make them superstars. For example, Warner recording Madonna, today a worldwide sensation, was an unknown two years ago.

But skyrocketing costs have made even baby acts risky. It costs anywhere from $125,000 to $250,000 to produce a pop album, roughly double the tab of five years ago. And promotion has also gotten more pricy now that music videos—film clips that dramatize pop songs—are considered essential. Thus, even a gold album—one that sells over 500,000 copies—can lose money. And not many baby acts exceed that volume on a first or second album.

"I personally lean toward developing baby acts, but the cost has gone up astronomically in the past five years," said Russ Regan, a top A.&.R. man at Polygram's Los Angeles office who literally gave the Beach Boys their name when he worked at CBS. "Today A.&.R. is much more cautious. The attitude is, you'd better make it the first time out."

Polygram has learned all too well the dangers of financial excess. In its rush to build a United States beachhead in the 1970's, it spent lavishly to buy market share. At first Polygram sold its records through independent distributors, but in 1972 it acquired United Artist's national distribution system. Over the next few years it gobbled up a number of record labels, including RSO and Casablanca. Polygram gave the entrepreneurial heads of these companies carte blanche to sign new acts.

In 1978, Polygram hit pay dirt. It issued "Saturday Night Fever" and "Grease," which sold an unprecedented 30 million copies apiece. The same year, disco became a national frenzy, and RSO and Casablanca seemed to corner the market with superstars like Donna Summer, the Bee Gees and the Village People. "There was a lot of euphoria," Mr. Hensler recalled. "All of a sudden, Polygram was right up there with CBS and Warner." It had become, recalls Mr. Dalhuisen, "the first record company in the world to break $1 billion in sales."

But by the end of 1979, the whole industry had hit the skids. Shipments of records in the United States declined 11 percent, the first such reversal since World War II.

All the record companies, Polygram included, had failed to impose limits on the number of unsold albums that the retailers could return, and by the end of 1979 they were buried under crates of black vinyl. "The whole industry had to eat an enormous amount of merchandise," recalled Russ Solomon, owner of Tower Records, a big national chain. "In fact, they're choking on it still."

Yet Polygram carried on as though the market were growing, not shrinking. Disco went the way of the hoolahoop, the Bee Gees and the Village People split up, and Donna Summer defected to Geffen Records. Polygram was stuck with its expanded distribution system. "We built a six-inch pipeline," Mr. Dalhuisen said, "to find out later that we could only fill it with two inches of product."

The Polygram labels contiuned to sign new acts. "They were signing everyone in sight," Mr. Braun recalled. "It wasn't as much taste as hope." Before long Polygram's United States roster had swelled to more than 250 acts—more than CBS has. Nearly all of them proved to be duds, and the cost of maintaining them was tremendous.

"Some people said it was just the distribution that was overextended and caused all the losses. That's nonsense," Mr. Hensler commented. "It was more a matter of obsolescence write-offs, shipping unlimited amounts of records. Casablanca went totally nuts." He added, "If I have 250 artists and only 10 are successful, and each of their albums costs me $100,000 or more before promotion—well, that tells you the story."

It fell upon Mr. Hensler to prune and consolidate. Aside from the cuts in distribution facilities and staff, he trimmed the artist roaster to about 80. To help pay back Polygram's huge debts, Mr. Hensler was also forced to sell the company's prized music publishing unit, the Chappel Music Company. Chappell, which was purchased by a group of investors last year for an estimated $100 million, holds the performance rights to thousands of songs, including a sheaf of standards by Cole Porter, Noel Coward and Rogers and Hart.

Now Polygram is ready to grow again, and to take risks once again. "You can't be in entertaiment software," Mr. Timmer said, "without accepting that it's a volatile business." Nonetheless, he insisted, "the company is going to be profitable from now on."

Mr. Asher is not quite so emphatic. "I haven't lost money in the past, and I hope to make money here," he said. "But after you've finished being smart in the record business, you also have to be lucky."

[From Variety, Jan. 26, 1985]

RECORD BIZ MAKES A STRONG COMEBACK

BUYERS RESPOND TO NEW MUSIC

(By Ken Terry)

After four long years of recession, disk biz finally began to see the light at the end of the tunnel in 1984. Through August, record retailers reported sales gains of 15–20%, and Christmas sales appeared to be strong enough to make those increases apply to the year as a whole.

Diskery product shipments also rose in the first half of last year, according to figures released in October by the Recording Industry Assn. of America. For the first six months of 1984, dollar value of shipment at list advanced 15% to $1.9-billion, while the number of units shipped by the labels jumped 18% compared with prior-year period.

These figures were mirrored in revenue and profit gains reported by some of the major manufacturers. Third quarter operating income for the Warner Communications Inc. Music Group, for instance, soared 54%, while revenues for the period jumped 27%. Similarly, CBS Records Group's third quarter earnings leaped 52% on revenues 15% greater than those in the same period of 1983.

FACTORS IN BOOM

Retailers cited a number of factors in the disk biz boom. Paramount, of course, was the national economic recovery. Dealers also mentioned the mass appeal of new releases, the lessening of competition from videogames, the growth of portable cassette player sales and the increased exposure of artists on MTV and other television outlets. Toward year's end, sales of compact disks also began to have an impact.

Most retailers warned, however, that an across-the-board increase in record prices would hurt sales. Evidently taking their accounts' advice, the majors raised list prices on only a handful of topselling titles.

As if to put its seal on the industry's newfound optimism, the RIAA made its first multi-platinum certification awards in early December. Not surprisingly, Michael Jackson's "Thriller" topped the list, with domestic sales of around 20,000,000 units.

The joker in the deck was the unexpected number of big selling albums that were not on the RIAA's list, as well as the fact that some labels chose not to participate. Behind the various excuses offered lay the possibility that some LPs might not have sold up to purported levels in previous years.

A somewhat sober assessment of the record business' past and its future prospects was released last month by the Gotham investment banking firm of Veronis, Suhler and Associates. The report noted that, despite the industry's improved position in 1983, as compared with 1979, it still had the slimmest pre-tax operating income margin of 10 communications industries surveyed.

A number of securities analysts agreed with one conclusion of the VS&A report: Record companies will have to keep costs down if they want to remain profitable.

MERGER K.O.'D

On the corporate level, the biggest single story of 1984 was the decision of WCI and Polygram to call off the worldwide merger of their recorded music interests. The two companies attributed the demise of their proposed deal to the intense opposition of the Federal Trade Commission, which felt the merger would give the WCI/Polygram entity too large a share of the U.S. record market.

The pact also had run into stormy weather in West Germany, where the Cartel Office had requested modifications in the agreement.

Polygram still is looking for a distribution deal with a major U.S. company; MCA and Capitol/EMI are said to have the inside track. Whatever happens, though, the European-based diskery plans to stay in the American market, as U.S. Polygram prexy Guenter Hensler stressed in a recent interview.

Despite the breakdown of the WCI-Polygram deal, another merger may be in the offing. Last May, RCA Corp. and the Bertelsmann Group of West Germany, already co-owners of Arista Records, said they were discussing the possibility of a joint venture or distribution pact between RCA and Bertelsmann's European record operation.

Since this combination would not dominate any national record market, it has not been viewed here as anti-competitive; however, no new moves have been revealed by the negotiating partners since last spring.

FEWER CHAINS, RACKS

While the pace of diskery mergers may have slowed last year, the trend toward consolidation into fewer, larger operations was never more evident in the retail and wholesale end of the business. Last May, for instance, Amarillo, Texas-based Western Merchandisers absorbed the music division of Salt Lake City-based Alta Inc., which included rack and one-stop concerns, as well as the Disc retail chain.

In October, the Ohio-based Camelot chain snapped up Franklin Music's four stores in Atlanta and one unit in Augusta, Ga., bringing its store total to 171.

And Handleman Co., already the largest U.S. rack jobber, made a couple of acquisitions in 1984 that further consolidated its position. In June, Handleman picked up inventory and rack fixtures from Pickwick Intl., later grapping many of Pickwick's former customers. The following fall, it completed a similar deal with Florida-based United Record and Tape, which signaled the latter's withdrawal from the rackjobbing business.

BIG TOURS

The concert scene in 1984 was highlighted by the tours of the Jackson, Prince and Bruce Springsteen. But, despite these top-grossing, recordbreaking roadtrips, the concert business as a whole apparently did not snap back with the resilience of the record industry (see separate story).

One of the more interesting phenomenon of last year was the emergence of the "video tour." Augmenting Thomas Dolby's U.S. tour last spring, for instance, a 90-minute package of clips and long-form videos was shown in rock clubs across the country.

More recently, rock club screenings of the Talking Heads' "Stop Making Sense" concert film were used to stimulate theatrical demand for the pic; significantly, the Heads did not go on the road at the same time.

The Heads were only one of many groups and artists who began to get or continued getting into pictures last year. Foremost among the musical performers who expanded into the visual media was Prince, whose role in "Purple Rain" made him a superstar.

Other prominent artists with feature film roles included Rick Springfield, Dolly Parton, Paul McCartney, Willie Nelson, Kris Kristofferson, Sting, Grace Jones, Patti LaBelle and Dee Dee Bridgewater.

Additionally, Madonna, Tina Turner and Mel Tillis were involved in upcoming pics, and such artists as Billy Idol, John Cougar Mellencamp, Dionne Warwick, Maurice White, Marlon Jackson, Diana Ross and Morris Day either were eyeing Hollywood or planning projects with studios.

There were also other tie-ins between the record and film industries. Capitalizing on the plethora of contempo music soundtracks, major film distribs began working ever more closely with labels on cross-promotions between the two media.

At the same time, music vidclips began rolling in theaters before features and studios started transforming trailers into music videos to be shown on MTV and other broadcast outlets.

While more videos were aired on more outlets than ever last year, MTV dominated the news and, in some ways, the music business. MTV play became nearly as important to the labels as radio airplay and, by the end of the year, most established acts and many new artists were making at least one vidclip for every new album.

Of course, this cost the labels a staggering amount of money, and not all of it could be recouped from increased album sales. At the same time, the diskeries couldn't just pull the plug on video production, which had become an essential part of their marketing strategies. So they began looking for other ways to make money from the use of vidclips.

Among other things, labels began to package clips into vidcassettes ranging from the three-five clip Sony Video 45s up to hour-length programs, some linking the videos with plot-like interludes. But, while music video sales have grown, they still form a fairly small part of the homevid business, with typical pertitle sales said to be under 10,000.

Not that the labels have given up on making music video into a profit center: The entrance of the CBS and RCA record marketing arms into the homevid business indicates these companies, at least, are intent on converting more record stores into video outlets. In addition, several labels have set up vidoe production arms, partly to encourage development of longform projects for the homevid market.

For the time being, of course, the diskeries' best hope of recouping their clip costs is to charge broadcast users for them. However, they've been slow to act in this area; evidently, they're afraid of restricting exposure of their artists' videos.

The only public agreement on payment for video usage last year was the controversial pact between MTV and four labels who, according to rumor, were CBS, MCA, RCA and Geffen. (Some other labels reportedly signed on later.)

In return for the payments, which MTV said would total $4,575,000 during 1984, the participating labels agreed to give the cable service exclusive broadcast rights to a portion of their videos for a specified period of time, said to be a month or more.

Naturally, other broadcasters screamed bloody murder, and one would-be competitor, the Coast-based Discovery channel (which has yet to launch its service), sued MTV over its exclusivity pacts.

Meanwhile, another entrant into the music cables sweepstakes, Turner Broadcasting's Cable Music Channel, began dickering with labels about paying for access to vidclips; shortly before it went on the air, CMC said it had access to videos from most labels. But it soon became clear CMC didn't have as many cable subs as it had first claimed, and it died before it could give MTV any competition.

CD PHENOMENON

Besides music video, the most ballyhoed new medium of last year was the compact disk. But it didn't really begin living up to its potential until the fourth quarter of 1984.

Back in January, the CD was still considered an elitist product. Players were selling in the $600 range, disks for $18-20. Fewer than 1,000 titles were available, the lion's share classical. Consumer awareness of the medium was said to be low.

But, as the year went on, hardware prices began dropping rapidly and, by December, low-end models were being advertised for as little as little as $200. Meanwhile, as the number of titles rose and worldwide pressing capacity was expanded, the prices of the digital-playback disks also started to fall.

In retrospect, the watershed was CBS Record's decision to discount wholesale on its CDs by 20% for the month of June. This move, later extended by CBS and imitated by other labels, eventually resulted in the lowering of CD list prices to around $15. On sale, CDs now sell for as little as $12.99.

As sales rose, labels began bringing out an increasing number of pop items on CD; at some point during the year, pop titles became a majority of available CD releases.

Then, around the end of last summer, the diskeries noticed their CD revenues were starting to build rather rapidly. During the first half of the year, according to the Recording Industry Assn. of America, some 1,500,000 CDs had been sold in the U.S.; by the end of 1984, per the chairman of the Compact Disk Group, Emiel Petrone, the labels had shipped around 4,500,000 units.

Outlook for the future of the CD is rosy, once the manufacturers solve the problem of inadequate supply. Only CD pressing plant in the U.S. is CBS/Sony's factory in Terre Haute, Ind., which started up last fall, but more are expected to open by 1986.

MISCELLANEOUS EVENTS

Other major events of 1984, briefly noted, include the following:

In August, Chappell/Intersong, the giant worldwide pubbery, was sold to a group consisting of Anglo-American Music and Edward B. Marks Music, both headed by Freddy Bienstock, Williamson Music and Wertheim & Co. No purchase price was announced for the deal, concluded late in the year.

Billboard, the music trade publication, was sold in November for around $40,000,000 to an investment firm, Boston Ventures, and a management group including the magazine's publisher, Jerry Hobbs, and Sam Holdsworth, copublisher of Musician magazine.

Capitol-EMI started a new U.S. label, Manhattan Records, with former Columbia and E/A exec Bruce Lundvall as president. The New York-based label made its first signings and revived the Blue Note jazz label.

MTV held its first music video awards in September; the big winners were the Cars, Herbie Hancock and Michael Jackson. The first international videoclip festival was held in St.-Tropez in October, but the promoters went belly-up after its trial run. City plans to carry it anyway.

While the Buffalo Broadcasting suit regarding local tv licenses continued to wend its way through the courts, Broadcast Music Inc. locked horns with radio broadcasters over an increase in blanket license fees. After two months of hardball tactics, BMI won, although it didn't impose as large an increase as it had wanted.

The major diskeries, in June, pulled the plug on the National Assn. of Recording Merchandisers' "Gift Of Music" institutional ad campaign. But some labels agreed to continue working with NARM on specific, event-oriented promotions.

Court victories by the Bee Gees and Michael Jackson in plagiarism suits may have discouraged songwriters from filing such actions in the future.

[From Variety, Apr. 10, 1985]

U.S. Record Sales Still Upward Bound

RETAILIERS HAPPY WITH 1ST QUARTER

(By Ken Terry)

Record retailers across the country report store-to-store sales gains of 10–20% for the first quarter of 1985. In most regions, the economy remains robust and consumer demand for prerecorded music product is stronger than ever.

This picture stands in marked contrast to the forecast of low '85 growth recently made by CBS Inc. CBS projected domestic industry sales would hit $4.51-billion this year, only a fraction of a percentage point more than 1984 volume.

On the other hand, as several dealers noted, CBS Records itself didn't do nearly as well in the first quarter as it did in the prior-year period, when its Michael Jackson LP, "Thriller," was setting world sales records.

According to the company's own figures, CBS Records Group profits for the three months ended March 31 fell 56% to $25,100,000 from $57,200,000 for the first quarter of 1984. Revenues dropped 17% to $292,400,000 from $350,700,000.

Although the Warner Communications Inc. Music Group has yet to release its first quarter report, most retail execs surveyed agreed the WCI labels are very hot right now, with topselling releases by such artists as Prince, Madonna and Phil Collins.

Compact disk sales are contributing more and more, also, to this retail bottom line. At Tower Records' 36 nationwide music stoes, CDs constitute 12% of record sales; they're 12% of overall sales at the Denver-based Budget Tapes & Records chain.

Elsewhere, the percentages are lower, but sales could be higher if CD fill were better. And, according to Tower chief Russ Solomon, more than half of CD volume is "plus business."

Nevertheless, Bill Forrest, financial v.p. of Elroy Enterprises, pointed out that, while CDs are the fastest-growing configurations at the TSS/Record World chain, they are not yet a "major factor" in his sales picture.

Since this is also true at many other chains, another explanation must be sought for the improvement in sales over the year-ago quarter when Michael Jackson was king.

VIGOROUS ECONOMY

Part of the continued market strength seems related to the vigor of the overall economy. In Detroit, for example, business is up 17% at the 16-unit Harmony House chain, which weathered the worst ravages of the recession.

Harmony House g.m. Jerry Adams noted his outlook for the rest of the year is "very optimistic. I don't see any dark clouds on the horizon. The auto business is good and that determines the economy in this region."

In contrast, John Marmaduke, prez of Hastings Books & Records, the 132-unit chain based in Amarillo, Texas, predicted 1985 "will not be a banner year like '84."

He cited the absence of a "Thriller"-level album and a steady decline of LPs in the marketplace; but, with regard to the first quarter, Marmaduke blamed Hastings' 5% store-to-store decline on a combination of "poor product, poor weather and the fact that we're down in the oil patch."

The latter factor seems to have taken a particularly heavy toll on business in the region affected by the oil industry depression. "There's more *empty* office space in Houston than there's office space in Philadelphia," quipped Marmaduke with grim humor.

Although Budget Records & Tapes enjoyed a 10–12% sales rise in the first quarter, chain topper Evan Lasky confirmed Marmaduke's assessment. "Among our stores, the ones that are struggling are in oil towns," he said.

RACK JOBBERS' OUTLOOK

Another sector of the industry that isn't faring as well as most of the chain retailers is the rackjobbing segment.

Lieberman Enterprises prexy Harold Okinow reported that for the fiscal quarter from December through February, "we're ahead, but that's because we added other stores." On a store-to-store basis, he said, "it's flat to a little down."

Okinow theorized retailers can do well when rack sales are flat "because our customer responds to something that's real hot." And right now, he averred, "There's no real burning hot product out there."

Nevertheless, he added, consumers "are ready to be tempted. The economy is no barrier to doing business."

Mario DeFilippo, v.p. of purchasing for Handelman Co., wasn't tremendously excited about early '85 sales, either. But he said Handleman projects an increase for the period after correcting for the addition of new accounts acquired from Pickwick and United Record & Tape last year.

"We're optimistic that our forecast will hold" through the company's fiscal fourth quarter, which runs through April, he said.

VIDEO SURGE

Many record retailers have placed a marked emphasis on video sales and rental in the past year, and in some cases, the results have been remarkable. Mitch Perliss, director of purchasing for Show Industries, which runs the 36-unit, Los Angeles-based Music Plus chain, said overall sales were 20% ahead of last year's first quarter, while record volume rose only 15%.

The effect of video can be measured by fact that last year, Music Plus had only two stores renting video and now has video in 21 outlets. "That's bringing a lot of bodies into the stores," Perliss commented.

Similarly, video now comprises 10% of Tower's overall business; video revenues have shot up 109% in the past year. Tower now has 26 video stores, either attached to or located inside record outlets.

Overall, per Solomon, Tower's first quarter sales were 33% ahead of last year's. On a store-to-store basis, March sales were 20% ahead, while the whole chain gained 43% compared with March 1984.

Camelot v.p. of purchasing Joe Bressi said his chain's first quarter sales were up 35%, but only 22% on a store-to-store basis. While record sales have been very strong, they now form only 70% of Camelot's business. Video, which was in 13 stores last year at this time, is now being sold and rented in 63 Camelot Music outlets.

Musicland, which enjoyed a 5–10% first quarter increase in its 360 stores, as well as the 75 outlets it operates under other names (Sam Goody, Harmony Hut), has found video business to be "spotty" this year, per Musicland Group topper Jack Eugster.

That seems to be partly related, however, to fact that only 12 of the chain's video outlets rent, while the rest sell—a strategy dictated by the stores' mall locations.

[From Variety, Apr. 10, 1985]

RIAA Metal Awards Show Increase in March

The Recording Industry Assn. of America certified five platinum albums, 10 gold LPs and three gold singles in March, an increase in all categories from March 1984's total of three platinum albums, eight gold LPs and two gold singles.

Multi-platinum titles certified last month include Grammy winner Cyndi Lauper's "She's So Unusual" (Portrait), which has sold 4,000,000 units, and Twisted Sister's "Stay Hungry" (Atlantic), which has moved more than 2,000,000.

Simultaneous gold and platinum awards were won by John Fogerty's topselling comeback, "Centerfield" (Warner Bros.), and REO Speedwagon's "Wheels Are Turnin' " (Epic), their fifth platinum LP. First-time platinum awards went to Julian Lennon for "Valotte" (Atlantic), Sheena Easton for "A Private Heaven" (EMI-America) and Phil Collins for "Hello, I Must Be Going" (Atlantic), certified gold in February 1983.

Gold album plaques went to Anne Murray for "A Little Good News" (Capitol), Kool & the Gang for "Emergency" (De-Lite), the Commodores for "All The Great Hits" (Motown), Ashford & Simpson for "Solid" (Capitol), Survivor for "Vital Signs"

(Scotti Bros.), Frankie Goes To Hollywood for "Welcome To The Pleasure Dome" (Island), and Philip Bailey for "Chinese Wall" (Columbia).

Winners of gold singles were Wham! for "Careless Whisper" (Columbia), the second gold single from their "Make It Big" LP, Foreigner for "I Want To Know What Love Is," and Philip Bailey & Phil Collins for their duet, "Easy Lover."

In the first quarter of 1985, the RIAA certified 20 platinum albums, 31 gold LPs and five gold singles, compared with 13 platinum albums, 35 gold LPs and five gold singles in the first quarter of the previous year.

In its certifications of non-theatrical videos, the RIAA recognized two music video titles in March: Lionel Richie's "All Night Long" (RCA/Columbia), which went gold and platinum in the same month, and Rick Springfield's "Platinum Videos" (RCA/Columbia), which went gold.

Within certain restrictions, the RIAA awards platinum certification to LPs selling 1,000,000 or more units, and makes multi-platinum recognition available for each additional 1,000,000-unit increment. Albums are certified gold at 500,000 units, while singles qualify for gold status with audited sales of 1,000,000 units.

Non-theatrical videos are certified gold at 20,000 units (with a suggested retail value of at least $800,000) and platinum at 40,000 units (with a suggested retail value of at least $1,600,000).

[From Variety, Oct. 9, 1985]

CBS, WB DEMAND MERCHANDISE RIGHTS

TELLER NAMED CBS DIVISION PREZ—SEZ THE LABEL IS IN GOOD SHAPE

Al Teller, promoted last week from senior v.p./g.m. of Columbia Records to prexy of the CBS Records Division, blames CBS' relatively low U.S. chart share this year on the fact that company's biggest acts have not been delivering albums by the dates for which they were targeted.

Although this has caused some problems in CBS' release schedule, Teller added, the company has tried not to pressure the artists, since its execs realize the creative process has its own timetable.

"Our anticipation is that 1986 will be better in terms of getting a more balanced schedule," he stated.

Meanwhile, he noted, CBS has given special attention to artist development, which has "paid off handsomely" with the breakthroughs of such acts as Paul Young, Wham!, the Hooters, til Tuesday and Dead Or Alive.

Teller sees no fundamental weaknesses in any area of CBS Records. "Over the past few years," he said, "CBS has shown excellent a&r, promotion and marketing strength across the board . . . If you look at the success the company has had over the past three to five years, it's quite strong and broad-based."

VIDEO CHALLENGE

The new CBS prez noted the diskeries haven't yet figured out how to recoup their investment in videoclips. "There's no question that the marketing economics carry a far heavier burden than a few years ago, and this is something the industry is still grappling with."

The only current solution, he pointed out, is to "hit a home run" with every record, which, of course, is impossible. Failing in that, he admitted, "the artist development process will continue to be very difficult" from a financial viewpoint.

In view of the added marketing and promotion costs, he said, "when you sign an artist, you have to prepare yourself for a major commitment." If the artist doesn't have a hit for a few albums, then the question of whether or not to retain him on the roster "becomes a little more complicated."

All of this means signing decisions must receive closer scrutiny than ever, noted Teller. But if this process becomes too rigorous, he warned, "you eliminate the cutting edge of music," and that will hurt the disk biz. "The industry must always be able to operate on the edge of where music is going."

OPERATIONAL CHIEF

As president of CBS Records Division, the company's domestic wing, Teller will have complete responsibility for overseeing the U.S. a&r, marketing and other functions of the Columbia and Epic/Portrait/Associated labels, as well as business affairs, sales and distribution and finance for the division.

Teller began his career in 1969 as assistant to the president, CBS Records Division, and in 1970 moved to Playboy Enterprises as director of corporate development. In 1971, he returned to CBS Records as director, marketing development, subsequently becoming v.p. of merchandising.

In 1974, he was named prexy of United Artists Records, and after a period on his own from 1976 to 1979, he joined Windsong Records as president.

He returned to CBS Records in 1981 as v.p. of operations on the staff of the deputy prez of CBS Records Group; later that year, he was named senior v.p./g.m. of Columbia.

Teller is the first individual to hold the CBS Records Division prexy's title since 1980.

[From Variety, Oct. 23, 1985]

WCI MUSIC GROUP INCOME RISES, BUT 3D QUARTER SALES DROP

Operating income of the Warner Communications Inc. Record Group for the third quarter, ended Sept. 30, rose 4% to $23,588,000 from $22,725,000 for the prior-year period. Operating profits for the nine-month period soared to $77,981,000 from $57,387,000 for the first nine months of 1984.

For the third quarter, Record Group revenues dropped slightly to $209,280,000 from $209,284,000 for the same period last year, confirming field reports of soft business conditions. Nine-month revenues increased to $642,157,000 from $566,286,000.

WCI Record Group includes Warner Bros., Atlantic and Elektra Records, WEA Corp., WEA Intl. and Warner Bros. Music.

[From the Washington Post, Nov. 24, 1985]

VANISHING ACTS: WHERE IS MICHAEL JACKSON?

(By Richard Harrington)

Remember Michael Jackson?

Skinny fellow, good singer, better dancer. A little weird.

Sold 38 million copies of his last record.

Inhabited newspapers, magazines and television for much of 1984.

If anybody has seen someone answering to this description, please call his record company and Rona Barrett.

What, you may wonder, *is* Michael Jackson doing? What d'ya mean, you don't care?

Pity poor Michael. Most people have to make comebacks from the lower depths. For them, a fall is to rise from. Jackson, the most public recluse since Howard Hughes, has to make his comeback from the most dizzying heights pop music had driven anyone to since the Beatles and Elvis Presley.

Exactly how *do* you follow up an album that sold twice as many copies as any other in the history of the known universe? An album that put your name on the lips of America and points east, west and south?

More important, how do you regain your credibility with a public that 18 months ago seemed willing to adore ad infinitum and then had its trust betrayed by a series of ugly commercial accommodations and terrible miscalculations?

Carefully, very carefully.

In 1984, you couldn't avoid Michaelmania. In 1985, about all you could do was miss it. In 1984, Michael's name was at the top of all too many column inches. In 1985, he's been an end note (injured once again while filming) or a business flash (spending $52 million for a song publishing company). His music has been limited to "We Are the World."

When Jackson announced after the final Victory concert (in a voice that sounded more aggressive than at any time in the last three years) that "this is our last and final tour," there was a certain relief. The burden of family obligations seemed thrown off and what was left was possibility.

But possibility for what? Michael Jackson may be the commercial phenomenon of the '80s, but he has yet to solidify or define his artistic position. His popularity has inspired imitation, but he's not been influential in the way that Prince has (just listen to the radio if you need proof). Jackson is a consummate craftsman in song or dance, but he has not made any real statements. The closest he came was during the Victory tour, when he issued a press release denying rumors that he was gay and threatening lawsuits against tabloids that pressed the issue. Of course Jackson didn't actually show up at the press conference to answer any questions, leaving *explications de tests* to his brand new manager.

The factoids are these: Michael is doing postproduction work on "Captain Eo," a 12-minute film (in stereo and 3-D) made with Francis Coppola and George Lucas for exclusive showings at Disneyland and Disney World. Michael is also doing preproduction work in the recording studio, sorting our songs for his next album (all originals) and waiting for producer Quincy Jones to finish his work on the film "The Color Purple." That album will be out in April.

What's evident here is that Jackson is receding even further into media that offer the greatest degree of self-editing and the densest walls to block out any real contact with his audience. Whether in the recording studio or on the set of a film, he can continue to refine his art without ever risking a performance. That's the prerogative of any artist, of course, but for someone already so out of touch with the real world, it bodes ill.

Like Sinatra, Jackson is a consummate performer, a genuine presence—but what he does in the studio doesn't always stand up under scrutiny. There's no great substance to "Thriller," a superb piece of pop calculation. That's the trick of cultural hysteria, to invest good work with an aura of greatness.

Let's call "Thriller's" follow-up "Exciter" (in the spirit that saw the recent Jacksons' albums titled "Destiny," "Triumph" and "Victory"). You know there's going to be all sorts of hypola when "Exciter" comes out. Say it sells 15 million copies. Will that be a disaster? Say it sells 45 million copies? Will that be a triumph?

And will anyone ask the real question—*is it any good?*

Prince did a shrewd thing with "Around the World in a Day," his followup to "Purple Rain," a record and film that eclipsed the Jacksons' Pyrrhic "Victory" celebrations and confirmed that the Michael supernova had begun to implode. "Purple Rain" had done all right—14 million records sold, $100 million at the box office, another $35 million or so on the concert circuit, additional tonnage from videocassette sales of both the movie and, more recently, concert footage. So how to sustain the momentum?

What Prince did was duck the issue of a quantitative follow-up to "Purple Rain" by making a qualitative follow-up. This is not to imply that "Around the World in a Day" was a particularly successful artistic achievement. But by making a significantly radical departure—neopsychedelia subbing for funk punk—Prince made moot the issue of sales figures (the album only did about 3 million copies) and replaced them with artistic questions. He looked in, not out, which was the response of an artist, not a music monger.

But Michael Jackson has an obsession with bigness that he may not be able to overcome.

Jackson is not the most eloquent artist, who ever lived, but he seemed absolutely self-assured when he said last year that "for the first time in my life, I feel like I've accomplished something." He wasn't talking about breaching the cultural apartheid of MTV and pop radio (which he did), or about making his liberating, form-bending videos. He was talking about selling so many copies of "Thriller" that he earned a line in (and delayed the press run of) the "Guiness Book of World Records."

This same obsession is evident in Jackson's current projects with Coppola, Lucas and the Disney organization (and to a certain extent with Quincy Jones). Work only with the biggest names, validate the bigness of the project and magnify the bigness of the ambition.

And don't worry about your roots, of course.

Certainly no one would point to "Victory" as any indication of new directions. Michael's involvement in that project was minimal—only two weak songs on an incredibly dull record—and it soon became obvious that art be damned, the family was simply out to gouge Michael's adoring public before the umbilical cord was severed. So why not charge so much that the Jacksons' original black constituency (through never exclusive) was virtually shut out of the tour?

"Thriller's" fans obviously included those who had helped Michael and his brothers sell 100 million records already. But the race ratios were almost turned around on the "Victory" tour, and what seemed to make Michael so interesting to the media—after 15 years of superstardom—was the crossover angle.

Yet as Dave Marsh points out in his new critical (and definitely unauthorized) biography, "Trapped," Jackson seemed oblivious to the implications of a black artist achieving such unprecedented popular acceptance—and was therefore unwilling to use that breakthrough to further integrate the top community. The stardom of Prince, Tina Tuner and Lionel Richie has done little to integrate the airwaves for lesser names; it's still a question of radio reacting only to the greatest public successes. Two years past "Thriller," nothing has really changed on radio.

Michaelmania was a self-induced hysteria, and folks tended to sink deeper into the instant mythology as Jackson proved increasingly elusive. But it's over now—largely due to the star's own abuse of his celebrity power.

In his few appearances at awards ceremonies (where he was usually sandwiched between date brooke Shields and chaperone Webster Lewis), Jackson seemed lost in the ozone, maintaining a Michael-as-child pose and refusing to make any significant or revealing statements. Those appearances were bizarre but also a bit endearing offering a glimpse of the innocent (albeit one who'd been a professional performer for 18 years) battling the weight of celebrityhood (invited as it was).

But the image began to turn sour with the Pepsi deal, in which Jackson sold the integrity of one of his best songs, "Billie Jean," for $5 million. Then came the Napoleonic "Victory" tour, with its Moscows and Waterloos at every turn. Much as Michael tried to disassociate himself from the rampant greed of "Victory," it tainted him so much that even when he gave his share of the loot to charity, it didn't rebuild his reputation (maybe the gesture was lost in the $60 million he'd made off "Thriller").

Even Jackson's participation in "We Are the World" was suspect. He may have written the song with Lionel Richie, but what you sensed from the various videos was that he had most definitely forgotten to check his ego at the door, Jackson was the only person to get special treatment on tape—a long, special effect shot reminiscent of the glitter of "Can You Feel It." He seemed aloof, indifferent.

Welcome to Celebrity Flameout.

Still, there remains a reason to care. Jackson's fall from grace—from 1984's pop culture hero to 1985's vague, inarticulate presence with much of his constituency gone—provides questions all pop megastars must face, about the process of celebrity and the responsibility of popular music. March's book, which tries to answer these questions—and ends up charging Jackson with a betrayal of both his art and his audience—comes as a welcome breeze of iconoclasm after a gale of iconography.

One can only hope that Michael reads it.

RESPONSES OF CHARLES D. FERRIS TO QUESTIONS SUBMITTED BY SENATOR MATHIAS

Mr. Ferris:

a- Music is at the heart of the blank tape and recording equipment industries. Without music, the industries you represent would not be as profitable as they are today. Nonetheless, we heard testimony indicating that by promoting home taping, these industries have jeopardized the future vitality of the music industry. How do you propose we respond to this problem in order to protect your stake in the music industry?

b- You have suggested that the recording industry has unilaterally decided to concentrate on the big hits and proven stars at the expense of the less popular artists or music forms. I presume that at least part of the motivation is the industry's desire to cut the losses it is suffering, partly as a result of home taping. You refer to this change in policy as an "efficiency measure." But is it a development that we want to encourage? Isn't the consumer going to suffer if home taping forces the recording industry to concentrate solely on the most profitable artists?

Future Vitality of the Music Industry

(a) First of all, I do not agree at all that there is a problem to which Congress must respond. By all accounts the music industry is very healthy. It is producing more music today than it has for years.

I also take strong issue with the contention that the consumer electronics industry has "jeopardized the future vitality of the music industry."

Our industry, which is being attacked by this legislation, clearly creates value for the record industry, and I continue to be perplexed by the failure of the RIAA to recognize this. Where would the recording industry be without our technology? Thanks to the portable music technology pre-recorded tapes now outsell records 2 to 1. This phenomenal sale of music in cassette form is in large part responsible for the excellent health of the music industry.

Furthermore, if the music industry took better advantage of the technology provided by our industry it could be even healthier. Take, for example, the new CD technology.

This new technology offers a tremendous opportunity for the record companies. According to Edgar Woodard, vice-chairman of DuPont (the world's largest supplier of Compact Discs), "Compact Discs currently comprise about 4% of the pre-recorded audio entertainment market, but by 1990 they are expected to account for 50% of that market."[1] Instead of preparing to meet this demand, the record companies are failing to invest in CD production. Just as they were slow to meet the demand for prerecorded cassettes and suffered for it, the record companies are mismanaging the opportunities created by CD technology. According to some analysts "twice as many Compact Discs could be sold as are currently produced."[2] As John Shulman, the general manager of Laury Records says, "The record companies can't even fill my orders now."[3] Even the vice-president of CBS Records admits, "It will take a very long time for supply to catch up with demand."[4] If the record industry does not take advantage of all the potential value and new markets we make available to them it is hardly our fault.

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[1] Billboard, Nov. 9, 1985, pg. 1.

[2] Id.

[3] Wall Street Journal, Oct. 24, 1985, pg. 1.

[4] Id.

The consumer electronics industry is concerned about the health of the music industry - so we are constantly adding to the health and wealth of that industry with our new technology. Rather than asking us about our stake in the music industry, I think we would all be better off if the music industry recognized their stake in our industry and worked harder to take advantage of new technology rather than attacking its source.

(b) The industry's moves to cut costs, by its executives' own admissions, have nothing to do with home taping. The industry's executives say the effort to cut costs is a result of the excesses they created following their peak year of 1978 when they thought the boom would go on forever. At that time, they made huge commitments, like increasing distribution networks, pressing more records, building more production plants, and signing more artists. "Record company spending was bloated by overstaffing, unrealistic contracts with some artists, and a general feeling that the boom times were going to go on forever. 'I think the industry had unfortunately become too imbued with the 20% growth pattern,' said Elliot Goldman, senior vice president of Warner Communications, Inc."[5] As a former CBS Records executive put it, "a lot of companies realized they were signing artists in a limitless fashion, based on the quality of the artist, rather than with reference to how many acts, especially new acts, the company could handle within a given period."[6]

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5. M. Potts, "Studios Grooving to Pop-Music Revolution," Wash. Post, Feb. 26, 1984, at G1.

6. P. DiMauro, "Disks Play Cautious Game; Once Burned, Twice Shy on Signing," Variety, Feb. 13, 1985, at 1.

As a result of these self-professed excesses and inefficiencies, the industry started to cut back. As a Washington Post article recently pointed out, "The cure was a series of cutbacks and consolidation moves at every major label. CBS' records division alone closed two record-pressing plants and half its regional distribution branches and laid off 20 percent of its full-time staff. The cuts left the companies lean and efficient and are resulting in big gains in profits even with modest increases in sales."[7]

Companies have also tried to be more selective about the artists they push and the records they release. With music videos costing from $25,000 to $250,000 to make and the overall bill for launching a new group ranging from $100,000 to $500,000, record companies have become more careful about releasing too many records.[8] Thus, the recording industry has learned its lesson from its excesses, and as a result has become a more efficient industry.

Further evidence of the industry's increased efficiency is the fact that the industry has succeeded in roughly doubling the hours of prerecorded music per employee. In 1984, each 1,000 music industry employees produced 20.14 hours of music while in 1972 the same 1,000 employees produced only 11.96 hours.[9]

So we have a more productive industry that by its own admission cut costs, not as a result of home taping, but because of excesses created by over-optimistic management. Now, industry executives are trying to blame fewer product releases on home taping. This argument just doesn't hold water. Indeed, the fact is that releases have gone up in 1984. Recently released RIAA figures show that the number of releases in all formats increased 9 percent in 1984. And if one were to take eight tracks out of the equation because they are now obsolete, the number of releases has increased 10 percent. (See attached chart.)

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[7] M. Potts, "Studios Grooving to Pop-Music Revolution," Wash. Post, Feb. 26, 1984, at G1.

[8] G. Fabrikant, "The Record Business is Solid Gold Again," Business Week, Feb. 25, 1985, at 35.

[9] Based on information taken from testimony of Alan Greenspan, Home Audio Recording Act: Hearing on S. 1739 Before the Subcomm. on Patents, Copyrights & Trademarks of the Senate Comm. on the Judiciary, 99th Cong., 1st Sess. (Oct. 30, 1985).

Increased productivity, increased cost efficiency. How could anyone argue that these are developments we don't want to encourage?

The Washington Post
Sunday, February 26, 1984
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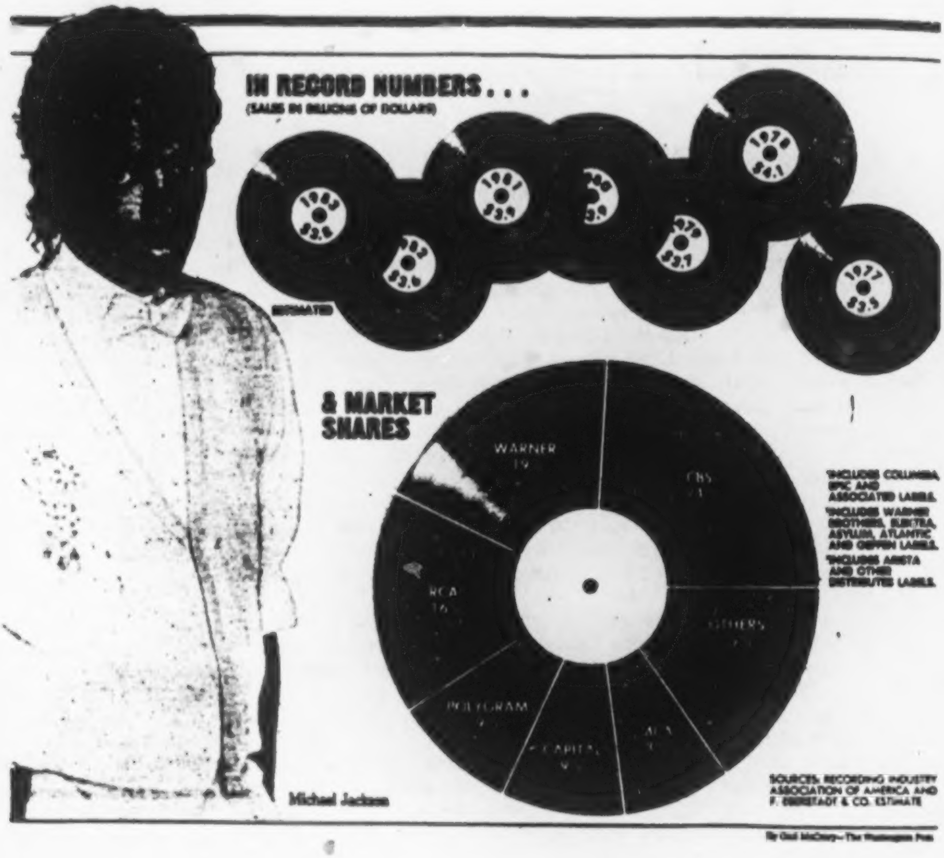

Michael Jackson

SOURCES: RECORDING INDUSTRY ASSOCIATION OF AMERICA AND F. EBERSTADT & CO. ESTIMATE

By Gail McCrory—The Washington Post

[From the Washington Post, Feb. 26, 1984]

STUDIOS GROOVING TO POP-MUSIC REVOLUTION

"THRILLER" ALBUM LEADS A SALES RESURGENCE UNEQUALLED SINCE GLORY DAYS OF SIXTIES AND SEVENTIES

(By Mark Potts)

If Michael Jackson's "Thriller" album sweeps Tuesday night's Grammy awards, as is expected, there's probably not a record company executive who will begrudge the young superstar's triumph.

Jackson has led a sales resurgence that may be returning the record industry to the glory days of the 1960s and 1970s, when everything it touched seemed to turn into a gold record—and then go platinum. And the rebound is not limited to rock music. Industry executives say they're seeing increased sales in all categories of music, from classical to country.

The phenomenal success of "Thriller," the biggest selling album of all time, symbolizes virtually every facet of a revolution taking place in the pop-music business; the return of the megaselling album, the renewed acceptance of black artists by all audiences, the loosening of radio formats that many record industry executives believed constricted artistic development for several years, and changes in mainstream tastes in music to "new wave" sounds or offshoots of "Thriller's" rock-disco dance beat.

Perhaps most significantly, "Thriller's" success illustrates the influence of music videos—promotional film clips that are spreading rapidly from frequent exposure on cable's MTV (Music Television) network to other outlets and into sales for home video players. Not only is "Thriller" the nation's best selling album, but a videotape of the making of the music video for the title song is No. 1 on the video sales charts as well.

But while CBS feted Jackson two weeks ago with one of the lavish parties in which the record business seems to specialize, the industry isn't throwing any parties yet to celebrate its own successful recovery. Burned by overoptimism in the past, industry leaders are waiting to see if the recovery will stick.

"The core question . . . is whether or not the resurgence of the record industry is a blip," said Robert D. Summer, president of the record division of RCA Corp. "There's some real good hard reasons to believe that the industry now has enough power to continue its climb."

Record sales rose 5 percent last year, after several years of doldrums, and are expected to increase by the same amount this year, although the rate of increase is still below the torrid pace of a decade ago. Industry executives and analysts say that, although hit albums are selling twice as well as they might have not long ago, sales of older albums are still flat. And the industry's 1983 estimated revenue of $3.8 billion still trailed the record $4.1 billion sales of 1978—the year the "Saturday Night Fever" sound track set the records that "Thriller" is breaking.

"Thriller's sales figures are amazing. In a business where a million-selling album is considered a big hit and earns a platinum award disk, "Thriller" has sold a whopping 27 million copies worldwide, according to officials of CBS Inc., whose Epic Records subsidiary makes the album.

Fifteen months after its release, the album is still selling at a 1-million-a-week clip—and that figure is sure to rise sharply after Jackson's expected Grammy sweep. "Thriller" also has produced seven hit singles—another all time high—and Epic officials are toying with the idea of releasing an eighth off the nine-song album.

There's only one "Thriller," of course. But industry officials say other hit albums, aided by many of the same factors, are selling much more briskly now than they would have a couple of years ago One analyst estimates that each of last year's top five popular albums—"Thriller," the sound track to "Flashdance," David Bowie's "Let's Dance," Def Leppard's "Pyromania" and Quiet Riot's "Mental Health" probably has sold in excess of 3 million records.

A couple of years ago, many in the record industry would have been happy with sales of a million or two from the biggest albums. The years between "Saturday Night Fever" and "Thriller" were generally not happy ones for the record business. The industry was hurt by the recession, by competition from video games, and by a dearth of exciting new music.

In addition, many potential customers recorded friends' albums onto cassettes rather than buying them—a bogeyman known as home taping that the industry still is grappling with.

The sales slump was a tough blow to an industry structured for growth. Record company spending was bloated by overstaffing, unrealistic contracts with some artists, and a general feeling that the boom times were going to go on forever.

"I think the industry had unfortunately become too imbued with the 20 percent growth pattern," said Elliot Goldman, the senior vice president of Warner Communications Inc. responsible for the company's Warner, Elektra, Asylum and other record labels.

"I think our cost base was too high," said Walter R. Yetnikoff, vice president of CBS and president of its record division, whose Columbia, Epic and other labels made it the industry leader even before "Thriller." "We overestimated the size of the market."

The cure was a series of cutbacks and consolidation moves at every major label. CBS' records division alone closed two record-pressing plants and half its regional distribution branches and laid off 20 percent of its full-time staff.

The cuts left the companies lean and efficient and are resulting in big gains in profits even with modest increases in sales. "Our cost base is significantly down, so when we have an increase in revenue, it falls to the bottom," Yetnikoff said. That's not to say the big-spending days are over—Yetnikoff recently signed the Rolling Stones to a huge CBS recording contract, the terms of which he won't discuss, except to downplay rumors that it was for as much as $28 million.

As the companies were addressing their internal problems, many of the external troubles began to ease: The economy improved, and the video game graze ended. And music videos and MTV arrived seemingly overnight.

"I think MTV has been a shot in the arm for the record business," Yetnikoff said. "If somebody had asked me three years ago, 'What do you think of an idea like MTV?' I would have said they were crazy. Fortunately, nobody asked me."

The music video is not an entirely new concept. Video clips of individual songs have been around for years, particularly in Great Britain, and can trace their roots to the great (and often not-so-great) rock and roll movies of the late 1950s and early 1960s, particularly the Beatles' "A Hard Days Night."

In its simplest form, a music video is a clip of a band performing a hit song in a concert setting. In more complicated videos, the artists portray characters in the song—or even play out a scene with little or no relation to the song's lyrics. Some of the most striking video art anywhere today appears in music videos.

Some artists are departing from the original format by extending the length of videos into the realm of the movie short—with Michael Jackson, naturally, leading the way: The video for the title track of "Thriller" runs 14 minutes and cost a reported $1 million to make, under the direction of John Landis, who directed the movie hits "Animal House" and "The Blues Brothers" and is one of many big-name movie and commercial directors to enter the music video field.

The most influential of the many outlets for music videos is MTV, the cable network part-owned by Warner Communications. It is given credit for having popularized videos—and for having made them a driving force in the promotion of records.

Playing videos 24 hours a day, MTV is performing a function similar to that of progressive FM radio stations in the late 1960s and early 1970s: finding and promoting new artists whose music might not be available to the public elswhere besides records. Some critics have grumbled that MTV can give a break to an artist better skilled at making videos than records, but there's no question about the network's power. Record industry officials credit MTV with virtually creating the careers of several major new artists, including the Stray Cats, Duran Duran and the Eurythmics.

MTV's definitely played a large role in "Thriller's" success. When the video version of "Thriller" began showing up on MTV and other video shows, the song quickly became one of the biggest hits on radio stations across the nation—even though it still hadn't been released as a single. When it was, its initial sale was one of the largest in history. "Michael Jackson has shown us that an exciting long-form video opens the way to some pretty important sales," Summers said.

Eyeing the success of music videos, record companies are scrambling to make them commerically available. "The Making of Thriller" is the first major commercial release of a music-video-related videotape, and it is being joined by "video singles," compilation tapes featuring several videos. It remains to be seen how many consumers will want to replace their turntables with CD machines and buy CDs—at $20 apiece—to replace their existing album collections.

MTV also is credited with playing a major role in the loosening of traditionally tight radio formats and the general acceptance of new wave music as a mainstream musical style. MTV featured new wave from the beginning—in part because new wave artists have made some of the most spectacular videos—forcing radio stations to begin playing the music, which usually features synthesizers, eerie vocals, or political messages.

And the Jackson phenomenon swept with it a number of black artists such as Prince and Lionel Richie, who are now receiving exposure on radio stations and video shows once completely dominated by white acts—a crossover not seen since the popularity of Jimi Hendrix in the late 1960s and the soul-music boom of the early 1970s. The proliferation of dance clubs also is aiding sales. Together with new wave, black rock-disco music is now a major factor on record sales charts.

Record executives see other reasons for optimism. Although the generation that grew up with rock music is now in its 30s—usually a time when record buying drops off sharply—the drop is not as pronounced for this generation. For the Baby Boomers, music "was an essential part of their being," Goldman said. "They're not going to walk away from music in their 40s and 50s." And their younger brothers and sisters are also proving to be big purchasers of records. "I think the demographics are in our favor," he added.

The industry is also enthusiastic about a couple of new technologies that are helping sales. The popularity of Walkman-type personal cassette players pushed overall sales of cassettes past those of disks last year for the first time—although it also may have exacerbated the home-taping problem by giving fans another reason to record favorite albums onto cassettes.

Another development, the compact disk (CD), with incredible sound quality produced by a combination of laser and digital computer technology, is seen as another new area for sales, although it remains to be seen how many consumers want to replace their turntables with CD machines and buy CDs—at $20 apiece—to replace their existing album collections.

So the record industry executive who will gather at Tuesday's Grammy awards ceremony in Los Angeles are cautiously optimistic, although they realize that the industry can't expect every album to be a "Thriller," or even to sell 1 million copies.

"You still have to get up every day and make sure that the 400,000- and 500,000- and the 800,000-sellers are still the ones that determine how you do your business," Goldman said.

"I think the music business is healthy," he said. "I see nothing, even in the bad days, that diminishes the need and the desire for music."

"People are not going away from music," Yetnikoff asserted. "It's got an emotional appeal that is apparently part of our biology."

[From the Variety, Feb. 13, 1985]

Disk Labels Play Cautious Game

ONCE BURNED, TWICE SHY ON SIGNING

(By Phil Dimauro)

Record companies may be flush with the profits of the year just ended, but a group of disk biz execs, entertainment lawyers and artist managers believe, for the most part, that improvements in cash flow are not likely to precipitate sharp increases in artist signings at most labels.

Exceptions to the rule mentioned most often are Elektra and Geffen Records, both of which recently expanded their a&r staffs, and MCA, which last fall announced a slew of signings while making its roster-building intentions known to the industry.

Even at the more aggressive companies, however, a&r departments continue to hold the line on variable cost items such as advances and recording budgets for new and unproved acts. While the cost of producing a videoclip for a new act was the reason most frequently given for cuts in other areas, industry observers also attributed a&r cost-consciousness to a general change in attitude that took hold after the major industry slump of the late '70s and early '80s.

The new attitude is really just common business sense, according to Dick Asher, a former CBS Records exec and music biz attorney who jointed the WCI Records Group as senior viceprez about four months ago.

Back when most labels were having financial difficulties, Asher said, "a lot of companies realized they were signing artists in a limitless fashion, based on the quality of the artist, rather than with reference to how many acts, especially new acts, the company could handle within a given period."

In their efforts to strike a more reasonable balance between product releases and the company's promotion and marketing potential, many diskeries trimmed artist rosters and cut their a&r staffs. The WCI vice-prez doesn't see record labels forgetting such tough lessons now or in the near future.

CAUTIOUS STANCE

His opinion was supported by entertainment attorney Elliot Hoffman, who observed that diskeries remain "circumspect in making deals" and "cautious about the extent of their investment" in artist signings. Hoffman said record companies have been granting smaller studio budgets than in the past, and keeping close tabs on recording expenses.

When considering new artists, labels are likely to offer "development deals, similar to what you'd find in the film industry," under which the diskery supplies demo money with a first refusal option rather than committing itself to an LP by an unproved act.

On the record company side, caution was leavened with optimism and enthusiasm. Lennie Petze, v.p. and senior manager of a&r for Epic and Portrait, for example, said he and his staff would be out on the road "looking actively for new artists this year."

Asked if his talent acquisition budget is higher this year, however, Petze replied that the Epic/Portrait staff hadn't even spent its entire budgets for the past two years. Questioned about how many new acts the company will sign in 1985, he stated, "We don't put a number on it."

Petze recently added one staff member on the Coast, Epic/Portait's first exec-level a&r appointment in three years. Staff, which now numbers five, had been up to 11 members during the late '70s, per Petze.

SENSE OF OPTIMISM

Other execs expressed varied shades of opinion on the signing climate. Polygram's Gotham-based a&r director, Peter Lubin, said the company's outlook had been bolstered by "a renewed sense of optimism in its ability to break artists . . . and the ability of the marketplace to absorb them," in contrast to the period two years ago, when it seemed a diskery had to "claw for every sale." But Polygram remains "careful, as we should be," per Lubin.

Talent scouts such as Geffen's John David Kalodner and Greg Geller, a&r viceprez for RCA, said the ups and downs in record company fortunes hadn't affected a&r attitudes at their companies.

Kalodner pointed out that the Geffen company had been launched in 1980, "the worst possible time" to start a few label in the opinion of some doomsayers. Geller observed that allowing slow sales to affect expenditures in talent acquisition, particularly for new acts, would be the best way to turn an industry slump into "an absolute disaster."

SMALLER ADVANCES

Kalodner said deals would remain "less heavy on the advances," in large part because videoclip production, now a virtual necessity, had become a major expense.

Even at MCA, where a&r viceprez Steve Moir said "right now, we really don't have any limitations," advances are a concern. "Our job is to make the best possible record," explained Moir, who said the record company doesn't want bands to "starve," but smaller advances make it easier to hold on to a new band when option time comes around.

The label recently has been pairing w.k. producers like Tom Dowd, Todd Rundgren and Keith Forsey with new acts. "If we have to pay a little more to get them," said Moir, "we will."

While bidding wars for new acts sometimes still occur (RCA's Geller suggested many are "concocted by clever record business attorneys"), nearly all insiders contacted said advances and studio budgets have shrunk.

Artist manager Eric Gardner, whose clients include Bill Wyman, Todd Rundgren, and Utopia, averred that advances for new acts, which he said had been up as high as $125–$150,000 three years ago, now tend to range between $65,000 and $80,000, a sacrifice most bands are more than willing to make in exchange for the all-important video budget.

[From Business Week, Feb. 25, 1985]

THE RECORD BUSINESS IS SOLID GOLD AGAIN

As Lennie Petze remembers it, when he first heard a tape of Cyndi Lauper, "she blew me away, I knew she would be hot." Petze, a vice-president of Portrait Records, a CBS Records label, was right. Lauper—a red-and-yellow-haired rocker who features her mother in her videos and manages Wendy Richter, the world's female wrestling champion—has become one of CBS's biggest stars. *She's So Unusual,* Lauper's debut album, generated five hit singles, sold about 4 million copies, and has been on the charts for 61 weeks.

CYNDI LAUPER'S FIRST ALBUM SOLD 4 MILLION COPIES AND GENERATED FIVE HIT SINGLES

Just three years ago, few albums sold more than 1 million copies or survived more than six months on best-seller lists. Lauper's success is just one sign that the once-troubled record industry is back in the groove. CBS/Records Group reported banner earnings in 1984, and its major rival, Warner Bros. Records Inc., is expected to report a strong profit increase. The two companies represent roughly 45% of domestic industry sales. While the industry may be unable to match its estimated 15% to 18% increase in sales next year, most record executives are bullish.

Much of the credit for the turnaround may belong not to the industry itself—or to better product—but to the popularity of Music Television (MTV), which has made it easier to promote established groups and make unknown singers household names. Don Zimmerman, president of Capitol Records Inc., also attributes the recovery to the revitalization of "top 40" radio. He points out that three years ago a lot of oldies were played on radio. But as a result of competition from the more daring MTV, stations are now airing more new records. That enables record companies to publicize a broader range of singers.

Movies with lots of music, such as *Footloose, Purple Rain,* and *Flashdance,* have also spurred sales. Prince's *Purple Rain,* an Atlantic Records release, sold 9 million copies, and *Footloose* has sold 5.5 million. Both yielded several hit singles. "Up until Michael Jackson, there was an unwritten law that if you got three hit singles off an album, God had smiled on you, and you'd better stop trying," says Barrie Bergman, chairman of Record Bar Inc., a large record chain.

Some companies are using the enthusiasm for superstars as an excuse to push through selective price hikes. Warner, for instance, just raised the suggested retail price of the newest Foreigner release, *I Want to Know What Love Is,* to $9.98, $1 more than is standard. "The industry has not had a price increase in over five years," says Geoffrey Holmes, a vice-president at Warner Communications Inc. "As a result of cost pressures on our margins, we raised the price." Nevertheless, the album has already sold 1.5 million copies.

ROAD TO BANKRUPTCY

Public resistance to widespread cost hikes could develop. But even if it does, industry experts ultimately expect that higher earnings from the burgeoning compact-disc business will offset any softening in vinyl profits. Holiday sales of compact discs were surprisingly strong, despite a $12.08 price tag. "The raw cost for a tape or a record is $1. We ship them for $5. CDs cost about $2.50, and we ship them for $8," says Holmes.

Warner Records has already put 300 of its 3,000 titles on CDs. Russell J. Bach, executive vice-president at Warner/Elektra/Atlantic Corp., says disc accounted for 5% of Warner's December revenues. Record companies also hope to build a market in music videos, the staple of MTV, on cassette. Still, it will be a while before compact discs or music videos add substantially to profits.

In the interim, the industry continues to stress cost-cutting, which became widespread when business slumped in the early 1980s. Retailers, for example, may no longer return an unlimited number of unsold records for credit from the manufacturer. And Record Bar President Ronald Cruickshank says the record companies have been attempting to get faster payments from retailers.

Companies are also trying to be more selective about the artists they push and the records they release. Music videos cost from $25,000 to $250,000 to make. The overall bill for launching a new group ranges from $100,000 to $500,000. To sign top performers, the companies are still willing to pay huge guarantees. But in general, "we try to release fewer records," says Atlantic Recording Corp. Chairman Ahmet M. Ertegun. Adds CBS Records President Walter R. Yetnikoff: "You can no longer just throw a record out there and hope it will stick. That's the road to bankruptcy."

If the economy remains strong and compact discs begin to take off, 1985 could be another year of ringing cash registers. For the record moguls, that's beautiful music.

[From the Wall Street Journal, Oct. 24, 1985]

COMPACT-DISK DEMAND GROWS FASTER THAN AUDIO SHOPS' SUPPLIES

The latest audio technology, introduced about three years ago, is catching on quicker than even its backers expected. That leaves the industry short of capacity to produce the plastic-and-metal disks for laser-based players. Polygram Records, a producer, says demand exists this year for 75 million to 85 million disks—compared with the industry's estimated world-wide capacity of 50 million to 55 million. According to retailers, the gap between supply and demand is widening. "I'm a little scared for Christmas," says John Shulman, the general manager of Laury Records, of Chicago. "The record companies can't even fill my orders now."

With U.S. sales of the players expected to double next year, the disk supply will probably stay under pressure. "It will take a very long time for supply to catch up with demand," says Jerry Shulman, a vice president of CBS Records.

[From the Billboard, Nov. 9, 1985]

PHILLIPS/DU PONT U.S. PLANT GEARING TO SHIP CD'S IN '86

MAJOR GOALS SET

(By Mike Hennessey)

NEW YORK—The Phillips/Du Pont joint venture company being formed to manufacture optical disks (Billboard, Oct. 19) will invest $50 million in building a production facility at Kings Mountain, N.C., which could be producing Compact Discs in time for the Christmas 1986 market.

The plant, to be installed in an existing 160,000-square foot building, is targeted to produce 25 million Compact Discs in 1987 and between 50 and 60 million in 1988. It is the first stage in a major investment program aimed at boosting CD software supplies to meet accelerating worldwide demand.

At simultaneous press conferences held here and in London last Tuesday (29), Phillips and Du Pont executives reported that the Phillips/Du Pont Opticals (PDO) venture aimed to bring its total CD production capacity to 200 million units by 1990 by adding facilities in other territories. By then total world production of CDs is expected to be in excess of 800 million units annually.

Between 1986 and 1990, PDO will make a capital investment of more than $500 million in optical disk production and will have an annual research and development budget of $60 million. It will eventually employ some 3,500 people.

Announcing details of the PDO venture at the New York press conference, Edgar S. Woolard, vice chairman of Du Pont, said it will be the world's largest supplier of Compact Discs for prerecorded music. It would have a turnover of about $1 billion by 1990, of which half would come from the audio CD and the rest from data applications or combination audio, video, data systems.

In the data area, PDO will be producing CD-ROM (non-erasable, read only memory software) and the CD-PROM type which can be programmed once. CD-ROMs, designed for use with personal and home computers, are expected to have their greatest demand in the business and instructional market. A single CD-ROM has the capacity of 1,500 floppy disks or about 250,000 typewritten pages.

The joint venture, the product of four years of negotiations between Du Pont and Phillips, represents a determined commitment to overcome the looming bottleneck in software supplies which Phillips, inventor of the CD system, contends could seriously damage the chances of the optional disks becoming the universally accepted audio and video carrier for home entertainment.

Some analysts assert that twice as many Compact Discs could be sold as are currently produced in the U.S., Japan and Europe, and with world player penetration expected to reach 80 million by the end of this decade, the need for more software production facilities is acute.

Jan Timmer, president of Poly-Gram, whose Hanover plant is currently the world's largest CD production center, (28 million units annually) has been trying for three years to encourage record companies to invest in CD production, "but," he says, "the response has been disappointing. The worst thing that could happen now would be for the spectacular takeoff of the CD system to be slowed down because of inadequate production capacity. That would be tragic. Therefore I am delighted by this Phillips/Du Pont initiative. Optical disks are a vital medium for the continued existence of the music industry."

Hans Gout, PolyGram's senior director of Compact Discs, who was present at the New York conference, said that PDO represented a commitment to the belief that the optical disk would be the ultimate, universal software system for the home "omni-player," which would incorporate audio CD, CD with video, a CD data system and 8- and 12-inch videodisks—an interactive entertainment and information complex, which would represent the most sophisticated marriage of audio and video.

Gout, who has played a key role in the international marketing of the CD system, is expected to be appointed director of sales and marketing for PDO.

"With home, in-car and portable applications," Gout said, "the CD has to be the universal carrier, and its versatility will reduce the incidence of private copying of prerecorded music."

PDO, which has inital assets of $150 million, will take over the Phillips video-optical plant in Blackburn, England, a product development center in Eindhoven, Holland, and the 51% stake Phillips has in the optical-media business of its venture with the Control Data Corp. in Minneapolis. PDO will also acquire an inital 50% stake in PolyGram's Hanover factory prior to taking total control. Plans are in hand for the expansion of the Hanover plant to reach an annual production capacity of 100 million CD units.

Du Pont's contribution to the joint venture will be a cash injunction believed to be about $60 million.

In addition, Du Pont will bring to the venture its optical disk facility near Wilmington, Del. and its access to the U.S. marketplace.

Woolard said that Compact Discs currently comprise about 4% of the prerecorded audio entertainment market, but by 1990 they are expected to account for 50% of that market, with cassettes taking 30% and "black" LPs 20%.

Referring to the videodisk element in the PDO operation, Woolard said it was not predicated on success in the consumer entertainment field but in the realm of instructional and educational programming. The new venture will market the Phillips LaserVison system and expansion of the home market is expected to follow the introduction of a combination CD, video and data system which Phillips is developing. Woolard revealed that the U.S. Army is planning to buy more than 50,000 videodisk players for instuctional purposes.

Another development in progress is the CD video single, a carrier for videoclips which makes use of the possibility of having up to five minutes of video on a Compact Disc.

The PDO venture will make a major contribution toward the achievement of the 6% penetration of the CD system in major markets, which PolyGram has always seen as the target to achieve the necessary momentum for the ultimate predominance of the Compact Disc. The process will undoubtedly be accelerated by the inevitable reduction in the retail price of Compact Discs which will go hand in hand with increased output.

Mr. Ferris:

The dubbing machines demonstrated at the hearing are marketed, at least in great part, as a means of reproducing copyrighted material.

a- Do you think that the line we have tried to draw between dual-port and single-port machines is a rational one? Don't these different machines have different implications for copyright, and shouldn't they be treated differently?

b- What do you think of our approach for redressing the infringements facilitated by the dual and multiple recording devices? Should we prohibit their importation once they pass a certain threshold (as this bill does with machines with three or more ports)? Or should we impose a graduated royalty based upon the number of copies that they are capable of producing? Say 25% for dual-headed recording devices, 50% for triple-headed devices, 75% for quadruple-headed recorders, and so on?

c- Would you agree that multiple-port machines are more likely than single-port machines to be used to make unauthorized copies of copyrighted works?

(a) Rationality of Line Between Dual Port and Single Port Machines

I think the line you have tried to draw between "single" and "dual" port audio machines is based on instinct rather than analysis, and won't hold up. I don't think the implications of dual port audio recorders are necessarily different, or, in the long term, negative.

Let's review how we got where we are today. In 1982 we told you that the recording industry had missed the market turn toward cassettes in several ways--availability, quality, merchandising--and that only the availability of blank tape and recorders allowed people to buy music and use

it the way they wanted. We pointed out that blank tape and recorders were helping to keep the music business competitive with Pac Man, who was eating up billions of teenagers' quarters that might have been spent on records. We commissioned the Yankelovich survey, which showed that typical taping of prerecorded music was for precisely this purpose--making the music more attractive and useful to purchase, rather than replacing purchases. At the same time, the Walkman and other portable players and recorders greatly expanded the situations in which music, on tape, could be played. Finally, the recording industry followed its customers and in a prosperous 1985 has sold about twice as many prerecorded tapes as they have records.

Is it any wonder that customers have taken this process one step further, and sought to enhance the utility of their prerecorded tapes? Most fundamentally, the dual audio deck makes the typical editing and "place shifting" purposes, which we have shown to be beneficial to copyrighted material, available in a market now dominated by prerecorded cassettes.

Unlike phonograph records and Compact Discs, tape is not a "random access" medium--you have to go through selections in the order in which they were placed on the tape. We know from surveys that much home taping is motivated by a desire to rearrange this order, or to take only a few selections from each album. Therefore, by providing the chance to rearrange or edit selections, the dual audio recorder compensates for one of the tape format's drawbacks, and enhances the home enjoyment of the tape that has been purchased--making such purchases more attractive. In a sense, this is similar to the basic "home" use of taping from records--to enhance enjoyment at home by guarding against degradation or damage.

With respect to portability, the dual recorder offers a similar enhancement. The jogger, motorist, and beach-goer, by recording favorite selections on 90-minute tapes, can take twice as much music along, including selections from many different prerecorded tapes. He can also mix selections from his record albums and his tapes.

Of course, records are not dead by any means and FM radio is more popular than ever. Therefore, the consumer who purchases a dual deck, instead of a single, will also use it for the same (beneficial) purposes to which he would have put the single.

Yes, we have seen the "smart-aleck" ads by a few catalog retailers, seized upon by RIAA, suggesting that these machines enable departures from established usage patterns. These ads were not placed by manufacturers. In my view they reflect the tongue-in-cheek marketing format of a few catalog houses (that don't specialize in audio or video) rather than the expectations of the manufacturers, which are based on careful analysis of usage patterns over decades.

(b) Approach in S. 1739

First, we are flatly and unequivocally opposed to any royalty tax, and for reasons given in (a) and (c) this applies equally to dual recorders. As to your question, I must say, respectfully, that the approach chosen strikes me as cockeyed and unworkable, and the alternatives you mention only compound the difficulties.

First, the definition of "dual audio recording device" is no sounder, or remediable, than the other definitions in the bill. Basically, it covers any device with a "cavity" for a digital or tape "phonorecord" and a "cavity" for a digital or tape "audio recording medium." Apparently, any "all in one" system containing a Compact Disc player and a tape recorder (as several new "boom boxes" do) is covered, whereas an integrated system containing a conventional phonograph is not. What learning is there that Compact Discs will be copied more "abusively" in portable units than on home component systems? Indeed, the 25% tax would be mostly on the value of the disc player (the most expensive element) when, in fact, by including the disc player in boom boxes, the manufacturer is making this format more portable, and less likely to be taped! The effect of the levy will be to keep Compact Disc players out of boom boxes, thereby encouraging consumers to tape CD's, to make them portable. This will result in a dollar-per-tape windfall for record companies, collecting on their own distortions of the market--a double penalty for consumers.

Looking to the future, the consequences become even more bizarre. Attached is an article from USA Today indicating that Kodak has developed a 12 megabyte floppy disc. This brings closer one of Len Feldman's predictions: that a contender for a multi-purpose digital recording format could involve high capacity floppy discs. Since most personal computers, including many intended for home use, have two drives, this means that any personal computer, using the multi-purpose medium, that is capable of copying from one drive to another will be a "dual audio recording device." Since this capability is fundamental to personal computers, this means that most personal computers with two high capacity storage systems (whether of optical, magnetic tape or disc, or solid state technology) will be "dual audio recorders."

Your more far-out suggestions simply illustrate the problems I discuss above--that singling out dual recorders will just create the dual problems of promoting taping and sharing new technology that the Congress does not wish to retard. By banning machines with "three or more ports" you never get to know what they will actually be used for. The CRT will have no way to judge, through user research, whether a multi-purpose, multi-port device is "intended for use in private homes." Does it take the manufacturer's word that it isn't--and thereby have triple port machines sell without penalty, while dual port machines are taxed at 25%? Or does it simply ban all such machines peremptorily, and let each manufacturer sue, armed with prospective market research, to get his machine on the market?

The graduated 25%-per head alternative would have about the same effect--the steep tax ensuring a technological detour, even a silly and inefficient one. All this, despite the fact that there have been no triple port recorders on the U.S. market[1] and the one model introduced in Japan has been scrapped.

(c) Likelihood for Copying

There are really two questions here--first, whether dual decks will be used more often to make "unauthorized" copies of prerecorded material, and second, whether their use is apt to be any less beneficial to copyright owners than is other recording at home. And, a third question should be asked: are such recorders any more apt to have significant or dominant uses that do not implicate copyrighted works, so would be most unfairly taxed? I think the answers, in order, are: not necessarily, not necessarily, and probably.

First, it should be recognized that, as all surveys have shown, the dominant use of all tape recorders is to play back prerecorded material. This follows a familiar pattern, observed in the video as well as audio: the recording feature of a player/recorder is what creates a market, which then is exploited and eventually dominated by software proprietors once they figure out the best way to deliver their wares to it. This trend appears to be only accelerating with the emergence of the dual audio recorder.

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[1] Some machines have triple playback capacity (A, then B, then C) but recording only involves two ports (A to B).

While Sen. Leahy expressed skepticism about the importance of the "sequential play" feature of dual decks, one should remember: a consumer who buys a dual deck in place of a single deck will use it mostly as he or she would have used the single deck--for playback, editing, or "place shifting." The sequential play feature is a way to carry more tapes inside the "boom box" or "Walkman" itself, as well as a way to have twice as much unattended playback (four times as much with 90 minute tapes).

Any extra amount of gross "taping" facilitated by dual recorders would seem to be proportionate to the enhanced playback opportunities. Moreover, the uses for home tape editing and tape place-shifting, added to the uses with non-tape source material, make dual recorders, like single recorders, machines that enhance rather than replace the purchase of prerecorded materials. Thus, while dual recorders are more versatile in the sources available, there is no evidence that they result in a greater amount of taping, or that their use is any less beneficial to copyright owners.

Finally, dual recorders also enhance the number of taping uses that have no relation to copyrighted material. These should be obvious. Tapes of children and family occasions, shown by the Yankelovich survey to be a major use of blank tape, can now be shared with relatives and friends. Music practice can be shared as well--indeed, the nation's tens of millions of amateur or semi-professional musicians now can make "demonstration" copies of tapes they have recorded themselves. This not only makes it more likely that recorders and tape will be used to make copies that have nothing to do with copyrighted material; the ability to make copies also increases the extent to which all recorders and tape will be used for home performance as an original use.

In summary, then, we don't think dual recorders are essentially different, can be treated differently, or should be treated differently. A tax on any recorders or blank tape would be a huge injustice.

Mr. Ferris:

Your testimony referred to the explosive growth in sales of compact disc players. Since at present it is not possible to record a CD using home technology, the problem of home audio taping from a prerecorded CD is distinguishable from the problem with regard to tapes since virtually all the materials on CDs are copyrighted. Is it appropriate for the companies you represent to encourage people to copy copyrighted material from CDs?

Compact Discs

The CD is one of the best examples of the recording industry crying all the way to the bank. Unable to manufacture them half as fast as they can sell them, making elevated margins on every sale, the record companies still find time to say home taping is a threat.

Like the devices that made a recording industry possible, the CD was not invented by an entertainment company--rather, it was invented and developed by the same industry that created the market for records and prerecorded cassettes.

One fact you should keep in mind: the recording industry's present prosperity is almost certainly understated on account of the shortage of CD stamping facilities. On the one hand, it is said that record companies could sell twice as many CDs if they had the capacity. On the other hand, frustrated owners of CDs are waiting to purchase their favorite music in this superior format (even though they might already own the record), and no doubt are passing up many records and tapes, to see if the same performance will be available in CD. That the industry should have missed the market in this manner, yet still be enjoying record sales and profits, attests to its underlying strength (and the overall beneficial effect of recording equipment and tapes).

There is no reason apparent why owners of CD players should be much different, in taping practices, from their practices with record players and tape recorders. There is less need to preserve the source material. But, compared with prerecorded tapes, the CD is still less portable, so will be taped more often for this reason. Overall, there is nothing to indicate that tape recorders will be any less complementary to CDs than they are to any other source material. Indeed, given the low price of CD players today and their extraordinary quality, many people will not accept any substitute for their combination of durability, quality, and programmability. Thus, taping will be most often for purposes of portability.

Mr. Ferris:

You indicated at the hearing that the recording industry is exaggerating the extent of their losses from the unauthorized home taping of copyrighted music. How much would you say they are losing?

Losses from Home Taping

The extent of losses from home taping claimed by the recording industry is based on an analysis first presented by Alan Greenspan in 1983 and resubmitted at the October 30, 1985, hearing on the Home Audio Recording Act. As is set forth in the attached critique of Greenspan's analysis performed by the firm of Cornell, Pelcovits & Brenner, this analysis was unreliable when first done and is of no value today in evaluating the advisability of adopting legislation in this area.

Additionally, merely looking at alleged losses from home taping is inadequate. Congress should take into account the fact that the consumer electronics industry and its technology, which is being attacked by this bill, have conferred great benefits on the recording industry. Weighing these benefits against any alleged harm from home taping, it is clear that on balance the recording industry is doing very well and neither needs nor deserves this tax.

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December 2, 1985

The Honorable Charles McC. Mathias
Chairman, Subcommittee on Patents, Copyrights and Trademarks
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

In his testimony on October 30, 1985, supporting passage of S. 1739, Alan Greenspan concluded by commending the bill as "a reasonable and creative response to the problems posed by the technology of home taping." Dr. Greenspan's testimony, however, fails to provide a complete or accurate analysis of the strengths and weaknesses of this proposed legislation. Hence, his overall assessment of the bill does not rest on an adequate foundation.

The bulk of his testimony was devoted to a relatively vague description of his estimate of how home taping has harmed the recording industry. This estimate is itself not reliable. In addition, his analysis ignores any consideration of the likely costs of imposing a tax on equipment (both the machines and the tapes) that are used for a wide variety of activities besides the taping at home of copyrighted music. Levying such a tax will cause distortions and impose costs on activities that do not even arguably have any impact on the creators of music. Moreover, such a tax will distort the development of technology both for home audio equipment and for these other activities that use audio tape. Dr. Greenspan's testimony completely ignored these issues.

Even when viewed from a very narrow perspective, namely the size of the possible loss to the recording industry from the advent of home taping, Dr. Greenspan's testimony is sufficiently flawed that it is not at all reliable. His analysis suffers from at least two major defects. First, the underlying model from which he calculates the degree to which home taping has displaced sales is based on unreliable survey data. Moreover, even had the data been reliable at the time the surveys were taken, enough has occurred since those surveys were taken that the data no longer is a good indication of home taping activity. Second, he has failed to analyze correctly the data on costs and employment in the recording industry.

The Economic Impact of S. 1739

An appraisal of the costs and benefits of any piece of legislation must look at the proposed bill and the effects it will have before any conclusions can be drawn about the wisdom of passing it. This Dr. Greenspan has completely failed to do. His discussion is cast entirely in terms of a model of the purported economic effects that home taping has had on the recording industry. While I believe (as detailed below) that his estimates of the effect are so flawed as to be unreliable, of even more importance is his failure to analyze at all the effects that the proposed tax would have on the numerous and growing uses for audio tape other than home taping, on consumers and businesses, and finally on the recording industry itself.

The proposed legislation would levy a tax of one cent per minute of playing time on every blank tape and an ad valorem tax of 5% on standard audio recording equipment and 25% on equipment with dual cassette recording capability. (The bill calls for the equipment tax to be waived if the machine had some device that made it impossible to tape from a prerecorded record or tape. No such technology exists, however, so this exception is academic, at least for the present.)

The legislation also contains a list of proposed "exemptions." Under these, the Copyright Royalty Tribunal could exempt certain categories of tape and certain kinds of purchasers. The CRT could exempt tape types that it determined were "unsuitable" for home taping of recorded music based on technical criteria. Also, particular purchasers could be exempted if they were purchasing tape or equipment for other than personal taping of recorded music. To exempt them, however, the CRT would have to establish some means by which purchasers could "certify" that they met the standards laid out in the bill.

A close look at the exemption provisions of the bill establishes that the intention is not to tax either users or uses of tape and recording equipment that do not involve recording copyrighted music. These provisions will not and cannot work. In its attempt to create exemptions, the bill tries to make two distinctions: between types of tape and between categories of users. The assumption behind the distinction between types of tape is that some audio tape is suitable for music and some is not. The distinction between users -- private versus business -- is based on the assumption that business users do not record copyrighted music but that private users do. Neither of these distinctions will serve the intended purpose, however. The distinction between tape types is invalid, while the distinction between types of users cannot be administered.

The fallacy that tapes can be distinguished based on their "technical" suitability or unsuitability for recording music is explained clearly in the testimony given by Mr. Leonard Feldman on October 30, 1985. (Statement of Leonard Feldman Before the Senate Judiciary Subcommittee on Patents, Copyrights and Trademarks on S. 1739.) What he said has been echoed by every other technical piece I have seen on this question. Despite allusions to companies' advertisements, all types of tape currently sold can be used for both music and non-music purposes. Moreover, as Mr. Feldman's testimony makes clear, the technology of taping and of tape is moving towards even greater convergence of a multiplicity of uses from a single type of tape. Under these circumstances, the CRT would appear to have no choice: all tape would have to be taxed no matter what the distortions to other applications and other industries.

Nor will the distortions be limited to industries that today use audio tape in one application or another. While the bill is written as if it would only tax audio recording media, the definition is vague enough to encompass video tape as well as audio tape. Indeed, video tape is a very high quality tape when used for audio purposes. If the bill were strictly enforced, the CRT would be required to collect a tax on all video tapes with the proceeds to be distributed to the recording industry. Such a tax would be far more costly even than if it were only levied on the audio cassettes. Moreover, because these types of tapes would be taxed under this bill, Dr. Greenspan's estimates of the likely receipts had the tax been in effect in 1984 are vastly understated.

Here, too, the tax would have impacts beyond the music world. Video tape and video recorders are used in a wide variety of applications that have no connection with music: in movie playback, home movies, and security monitoring in office buildings and stores, to name just a few. Yet, these uses would find themselves burdened with a tax that was intended to correct a "problem" those users had no hand in creating.

Moreover, this distortion is likely to grow quite rapidly. With the exception of music videos, current video tape is not widely used for what is actually an audio purpose. The technology here is changing, however. The new eight millimeter video tape and equipment is being described as suitable for both pure audio and the whole range of video purposes, as discussed in some detail in Mr. Feldman's testimony. Thus, even if the CRT were to grant an exemption for the existing versions of video tape, they would be unlikely to do so for eight millimeter video. Yet this technology promises a wide range of new applications once users get accustomed to being able to work with much lighter and smaller components. All of this activity could be slowed or distorted by the imposition of this tax.

Given that all tape types would have to be taxed, the second category of exemptions called for in the bill would be the only means of trying to limit the impact of the tax to those who are using tapes and equipment for recording copyrighted music. Again, however, the distinctions being drawn will not serve their intended purpose with any degree of precision, and to whatever degree they do succeed in insulating some users from the tax, the cost of doing so will be very high.

The bill itself is silent about the mechanism the CRT should use to exempt business users from this tax. In its testimony in support of this bill, the RIAA suggested that "[qualified purchasers will likely secure royalty-exempt tape and equipment directly from the manufacturers or through specially-placed orders with retailers." (Joint Statement of National Music Publishers' Association, Inc., Recording Industry Association of America, Inc., and Songwriters Guild of America Re: S. 1739, The Home Audio Recording Act, October 30, 1985, p. 55-56.) What the RIAA is saying is that they believe that two completely separate distribution systems, one for residential consumers and one for business, will develop.

In simple terms, this means that a business user located next to a record and tape store who finds himself suddenly in need of another box of cassettes will have to either pay the tax or go to a more distant location to avoid the tax. While to some extent the distribution systems are separate today, the separation is not complete. Nor should it be forced into that mold. The costs of forcing such a separation are sheer waste.

RIAA's recognition of this as a possible outcome demonstrates that they believe this bill would impose potentially very high costs on those who have no impact whatever on the recording industry. No longer will stores like Ginn's be able to quote a single price to all users of a single cassette; they will have to quote different prices depending upon whether the item is "specially" ordered or not. As anyone who has bought supplies should know, special orders are more costly than regular orders because of the extra paperwork and handling special orders require.

The RIAA's version of how the exemption would work would indeed impose these extra costs. The paperwork required to establish that one is a "qualified" buyer could be sufficiently costly that it would not pay to try to qualify for the exemption. The extra burdens are certain to have this effect on at least some business users, particularly those who buy in relatively small quantities at one time. While each such user's purchases may be small, nobody knows what percent of total business tape purchases would be involved. Audio tape has a wide range of uses. Some types of photocopy equipment use cassettes to keep track of billing information. Some small computers use cassettes to hold data and programs. Court reporting equipment often uses cassettes as either the only or one of several means of recording a proceeding. These are just a few examples. Others are given in Mr. Feldman's testimony.

The net effect of this legislation would be to send a signal that it would be better to find an alternative means to achieve the functions that audio tape serves in these uses. If an alternative means were just as effective and efficient, however, it would already have been developed. The fact that audio tape cassettes were chosen means that the tax will push the technology to an inferior alternative, at least for some period.

Moreover, the problems inherent in trying to use this exemption provision to shield uses that do not involve audio recordings of prerecorded music will be overwhelming once eight millimeter video is included. Because many of the applications of this technology will be intended for use by residential consumers, the problem cannot be avoided even cosmetically by the development of a dual distribution system. That "solution," however expensive, is only available at all when distinctions can be made on the basis of the identity of the users. In this case, however, many more of the users would be indistinguishable; only their uses would differ.

Still another problem with the tax would be its impact on the equipment consumers buy in the future with which to enjoy music at home. The proposed tax is 5% of the wholesale value of the recording device. The bill is silent about what to do if the recording device is part of a complete stereo system. Is the wholesale value the value of the whole combined device, or must some mechanism be established to determine what share of that value to attribute to the recording capability versus all the other parts? If the CRT must hold hearings to determine what fraction of the wholesale price to attribute to the taping capability, the cost of combining functions into one piece of equipment will rise relative to the cost of producing separate components. If the entire wholesale value is taxed, the purchase of combined audio equipment will rise sharply in relation to the prices of separate components. In either case, the bill will artificially distort the choice in the market of combined versus component music systems.

Given the RIAA's own implicit recognition of the high cost of this bill on areas that should not be taxed because they clearly are uninvolved in any purported harm, Dr. Greenspan's silence on this aspect of the bill he supported is disturbing. At a minimum, he should have demonstrated that the bill offers net benefits to society despite these high costs. Given his own belief that the proposed tax would raise only $200 million, does he believe that raising that amount is worth the substantial dislocation in areas that do not even arguably contribute to the harm that supposedly is being compensated? It seems hard to believe, however, that he would view as unimportant the high costs of distorting technology, particularly future technological change.

To a very considerable extent, future gains in productivity depend upon technological change. Distorting it, by taxing it, thus slowing its deployment, or by pushing it into more costly paths in order to avoid a tax, should be done only when the benefits outweigh the costs. Dr. Greenspan simply did not address these issues. Instead, he was content to present his estimate of the harm the recording industry has suffered due to home taping. That estimate, however, is unsupportable when examined more closely.

The Problems with Greenspan's Damage Estimate

Dr. Greenspan's estimates of the losses suffered by the recording industry in 1984 are shown in Table 5 of his testimony. Ostensibly, he offers two methodologies, but in fact both depend on the same data and assumptions, so they are not independent means of arriving at an estimate. Both use data on blank tape sales, old survey estimates of the fraction of home taping that involves copyrighted material, old survey estimates of the fraction of home taping that displaces sales of prerecorded music, and an estimate of how many albums can be included on a tape. Dr. Greenspan uses these elements to construct two very similar estimates of the lost retail sales of prerecorded music due to home taping. The numbers upon which he builds his estimates, however, do not stand up to closer examination for two reasons: their age, and their inherent unreliability.

The basis for much of his estimates comes from two surveys. One in particular, the Warner Survey, is about five years old. Its data derive from an era when the recording industry released only a fraction of its titles on prerecorded cassettes, and those that were released were often put on the market significantly after the record of the same music had been released. Yet, this era also marked the beginning of the rapid spread of the truly portable tape players -- the Walkman revolution. The rapid spread of the players demonstrated that people wanted to be able to have portability as part of their music listening. The Yankelovich survey confirmed this market evidence. With the recording industry not providing many of its titles on prerecorded cassettes, and with music stores not aggressively marketing them, consumers turned to a time-honored American tradition: self-supply.

Today the recorded music market has recognized this change in taste. According to RIAA's own statistics, 1982 marked the first year that there were as many new releases on cassettes as on LPs. Cassettes are now as readily found in and marketed by music stores as records. Perhaps for this reason, blank tape sales have essentially been flat over the last year. These conditions suggest that home taping behavior is likely to have changed in the years since the Warner survey was taken.

Even if there had not been a change in the market and in the way people use home taping equipment, however, the numbers that came from the old surveys do not stand up well under close scrutiny. Nor do some of the other elements from which Dr. Greenspan built his estimates of harm. Moreover, in all cases where Dr. Greenspan had a choice of numbers, he made a consistent choice: the highest.

Dr. Greenspan's first estimate is built up from the number of blank tapes sold. There is no agreed source for this statistic; Dr. Greenspan has chosen the highest estimate of blank tape sales to do his calculation.[*/] He then multiplies this by a factor, 0.75, to derive the number of tapes that were used to tape copyrighted music. This factor comes from the Warner Survey conducted in 1980. The number represents the fraction of tapes bought by interviewees that were used to tape copyrighted music. Again, he has chosen the highest estimate of this factor. The Yankelovich survey found that number to be just less than 0.5.

Even if the Warner Survey estimate were accurate, it is not the right number for Dr. Greenspan's purpose. The respondents in the Warner Survey were not a random sample of all tape consumers. At best, they were a random sample of residential consumers. Much tape is sold to businesses, but businesses were not interviewed. The fraction of total residential consumer purchases used for taping copyrighted music at home thus cannot be applied to total tape sales, including sales to businesses, to estimate the amount of tape used to record prerecorded music. Dr. Greenspan's method clearly results is a substantial overstatement of the tape used to record prerecorded music. Surely far less than 75% of the blank tape purchased by business

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[*/] Dr. Greenspan used an estimate from Merchandising for his figure of 1984 tape sales, 263.9 million units. (Table 5, line 1) In his calculation of the take of the tax, however, he uses a different number, also from Merchandising of 261 million (Table 8, Note (b)). The data collected by the International Tape/Disc Association, however, gives sales of 243 million units, while the Electronic Industries Association reports sales of only 228 million units in 1984.

is used in this way -- indeed, it is doubtful that any significant amount of blank tape purchased by businesses is used to record copyrighted music.

What fraction should be applied to total tape sales is unknown, but it is instructive to look at the numbers Dr. Greenspan used to estimate the total revenues to be raised by a tax on blank tapes if one had been in effect in 1984. For that calculation, Dr. Greenspan assumed that approximately 45% of total tape sales were of tapes that would be "technically unsuitable" for taping music. Moreover, Dr. Greenspan further adjusted the remaining quantity of tape that would have been subjected to the tax by exempting 11% of that remaining 55%, resulting in his calculating that only about 49% of total tape sales would have been subject to the tax. Either Dr. Greenspan has seriously underestimated the total amount of tax that would have been collected in 1984, or he is conceding that the total amount of taping of copyrighted music is much less than 75% of total tape sales.

The next step in Dr. Greenspan's estimate of the amount of harm done by home taping of copyrighted music is also flawed. Having estimated the total number of blank tapes used to record prerecorded music, he then took a factor, 0.426, from an Audits and Surveys study to compute the amount of that taping that displaced a sale of prerecorded music. The Audits and Survey questionnaire asked people whether, if they had not made the tape, they would have bought a record or prerecorded tape of the piece instead.

This factor, too, is unreliable and almost certainly significantly overstated. The survey made no check to ensure that the people who said taping displaced purchases could have bought the same music they had taped. Since a high proportion of home tapes are of selections rather than complete albums, home tapes frequently would be unable to buy a tape comparable to the ones they record. By ignoring this, the survey -- and Dr. Greenspan -- clearly overstate the displacement effect.

Moreover, asking people what they might have bought is well known to produce unreliable answers. People are always more willing to spend hypothetical money for hypothetical purchases than they are to spend real money for real purchases. Indeed, people tend to overestimate how much they actually have spent when asked for this information in surveys. A good example is found in a survey commissioned by the RIAA from the Roper Organization in 1979. In that survey, respondents reported that they had bought 164% of the actual annual sales of LPs for the previous year.

The Audits and Surveys study made no attempt to correct for either problem of inaccurate responses. Neither did Dr. Greenspan. As a result, the factor he used is overstated.

Dr. Greenspan next had to convert cassettes into album equivalents in order to be able to compute an estimate of how many albums would have been sold if there were no home taping. To do this he used 1.875 albums per blank tape, based on the average number of minutes per blank tape versus the average number of minutes of music on an album.**/ Having converted the number of tapes that displaced a sale of an album into album equivalents, Dr. Greenspan concludes his Table 5 estimate under his Method I by multiplying that number by the average price of an album in 1984. This is the basis for his estimate of the gross loss in retail sales of prerecorded music due to home taping.

In the text of his testimony, he admits that not all of the loss in gross sales is compensable. Some represents costs that

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**/ This number is also overstated, however, although it is not clear by how much. Despite the broad averages, people who tape do not end a tape in the middle of a selection just to use every minute of tape. People tape whole selections, even if that means leaving part of a tape blank. When people tape entire albums, a substantial amount of the tape can be left blank.

the industry saved by not making the sales. Dr. Greenspan relied on his own model of the margins of the recording industry to claim that the industry should be receive compensation of approximately two fifths of the retail price.

It is not possible to analyze this model of industry margins, because Dr. Greenspan did not reveal either the data used, the model itself, or its actual results. It is noteworthy, however, that Dr. Greenspan did not compare the margins of the recording industry with margins in other, competitive industries. This, not some time series of the margins over the years, would be a more appropriate measure of the state of the industry. Is it an industry in which investors want to invest, or is it one in which capacity is declining? Dr. Greenspan did not provide either opinions or data that address these questions.

While Dr. Greenspan did not give any actual results of his model of industry margins, the figure he derived for compensable losses, about two-fifths of the retail losses due to home taping, is clearly too large. Dr. Greenspan stated that he included the "incremental royalties and income that would have been earned by recording artists, composers, publishers, musicians' and performers' unions, and recording companies." (Testimony, p. 11) By including all of the incremental income, however, he is including a payment for services and investments other than the copyrights. Such investments include warehouses, recording equipment, and inventories of parts, for example.

This is clearly illegitimate. Surely even those who favor a taping tax would not argue that consumers must only consume music that is recorded by those who form the current industry. The whole spirit of the bill is that if consumers pay a tax for copyright purposes, they should then be free to tape at home. Under the theory of this bill, if purchasers of blank tape and tape recorders have compensated copyright holders for the copyright through this tax, then they would be free to make their own reproductions if they prefer them to those of recording companies. There is no reason, however, that consumers also should have to pay recording companies for their investments in pressing plants, distribution facilities and so forth if consumers instead prefer to use their own home reproduction facilities. There is no reason the bill should guarantee to recording companies returns on these investments, any more than any other industry is guaranteed returns on their investments if consumers turn to alternative suppliers, including homemade equivalents.

Yet Dr. Greenspan's numbers include lost profits beyond the lost royalties, counter to the spirit of the bill. Based upon these calculations, Dr. Greenspan is calling for the tax not only to compensate copyright owners but also to support the profits of the recording companies. (He may also be including support for the profits of retailers, as he uses the retail, not the wholesale price, as the basis of his estimates. Again, without having the analysis to review, it is not possible to know whether this is an additional overstatement.)

Dr. Greenspan further supported his claims of harm to the recording industry with two tables, one showing the downward trend in employment in the industry and the other showing that the price for an album has declined relative to the Consumer Price Index. The fact that both employment and prices have fallen, he claims, is further proof that the recording industry has been injured by home taping. Elsewhere in his testimony he claims that costs are relatively fixed in the recording business.

There is a very different -- and likely more accurate -- interpretation of these data. When the employment data are put together with the output data, the ratio demonstrates strongly that productivity, as measured by hours of prerecorded music per employee, has almost doubled from 1972 to 1984. (See Table 1.) Such changes in employee productivity are inconsistent with the image of an industry that has unchanging costs. Rather, productivity increases of this magnitude usually imply a change in production technology that has brought about lowered labor costs per hour of prerecorded music.

Moreover, the period in question was a period of stable or falling real wages in the U.S. economy. Unless the employees of the recording industry were vastly different than their counterparts in other industries, the recording industry thus had a double benefit: less labor needed per hour of prerecorded music combined with stable costs for an hour of labor. Under these circumstances, if the industry is competitive and not experiencing some unusual cost pressures other than from labor costs, prices would be likely to decline relative to other prices in the economy. In short, neither of his supporting data series necessarily provides any support at all for his argument. The falling prices seem more consistent with an industry that has undergone significant cost-reducing technological change. Nor does falling total employment necessarily represent anything except increased labor productivity.

Conclusions

In summary, Dr. Greenspan has endorsed a bill whose real costs he has not acknowledged. These costs are likely to be high: distortion of the future direction of technological change, higher costs of performing a number of business operations, and the loss of a number of consumer benefits from emerging tape technologies that can be, but are not always or even predominantly going to be used to tape copyrighted music. These costs should be one of the central considerations in evaluating this legislation.

Even if it were correct to ignore all the costs and focus only on the harm being done, Dr. Greenspan's analysis does not support the conclusion that this bill would be wise public policy. Dr. Greenspan has certainly overstated the harm by a very large magnitude.

The result of Dr. Greenspan's overstatement of the losses and the failure to take into account the much broader reach of the tax, particularly its likely imposition on video tape, mean that his conclusion that the bill will raise an amount that, "falls far short of the sum that I believe should be compensable to copyright owners and creators," is almost certainly wrong. (Testimony at p. 12) This bill would very likely create more injury than whatever harm it is intended to redress.

Sincerely,

Nina W. Cornell

Nina W. Cornell

TABLE 1

Year	Hours of Prerecorded Music per Employee (000)
72	11.96
73	11.07
74	11.59
75	11.65
76	11.26
77	13.34
78	13.05
79	13.13
80	14.68
81	13.50
82	14.90
83	16.21
84	20.14

Mr. Ferris:

S. 1739 provides an exemption to machinery containing technological innovations to prevent unauthorized home taping.

a- Please assess the status of the technological solutions that are being developed to "encode" the various tools used to copy audio materials.

b- Can we expect the market place to respond to the unauthorized home taping of copyrighted material? If so, please estimate how much the encoding mechanisms would add to the consumer's cost per machine.

c- Is it true that the manufacturers of recording equipment have refused to discuss with the recording industry the use of an encoding system that would provide a viable market place solution to the problem of unauthorized home audio taping? If not, please describe the status of these discussions?

d-- At the hearing I invited anyone interested in this problem to recommend alternatives and amendments to S. 1739. Someone suggested legislation that would require all audio recording devices and all prerecorded phonorecords of every medium distributed after a given date -- for example, January 1, 1988 -- to contain the appropriate encoding mechanism. What is your reaction to that type of legislation?

Technological Encoding

(a) Status

Insofar as we are aware, there is no way to make a tape that can be played back but not copied. We have not investigated the "subliminal signal" system involving microchips, discussed by Mr. Gortikov, because it would be an unwarranted burden and intrusion on consumers. The entire concept is shallow and partial--why not have a device that monitors each time a prerecorded tape is played back on a

recorder, so the copyright owner can pay an appropriate patent royalty to the recorder manufacturer?

(b) Marketplace

The marketplace will never demand or tolerate the totalitarian approach to home taping. People cherish their freedom to use items they have bought; they will never enjoy a personal purchase that is limited in such a frustrating and unnecessary way.

We do not really understand how a system as described by Mr. Gortikov could work, so we cannot estimate its expense. A system limited to disabling encoded recorders from making copies of encoded phonorecords would disable recorders from fulfilling the portability and editing functions so important to consumers. Also, experience has taught that any encoding system in a recorder can be easily bypassed, unless it is itself prohibitively expensive. And a system that could "meter" and "tote up" charges for each copy would be so devoured by technical and transaction costs it would be impossible. Either way, the marketplace would not tolerate such a system.

(c) Recording Industry "Proposal"

The claims of the RIAA in this respect can only be described as insincere and self-serving. Our understanding is that in 1983 Mr. Gortikov and other industry leaders approached executives of Japan's electronics industry with a plea to discuss recorder-disabling technology. The leaders of the industry in Japan responded that they refused to discuss matters related to legislation in the U.S. behind the backs of this Coalition. The RIAA executives replied with assurances that they did not wish to discuss any matters pertaining to the legislative situation in the U.S. The Japanese leaders then declined on antitrust grounds. But Mr. Gortikov, despite the assurances that the discussions would not relate to legislation in the U.S., proceeded to tell the Congress that he had proposed discussing such legislation!

While ARRC has never been approached with such a proposal, we would not be interested. As we have shown, the typical use of blank tape and recorders is beneficial to the use of copyrighted material. We see no reason for manufacturers and the recording industry to join in an assault on their common customers.

(d) Legislation for Mechanisms After Jan. 1, 1988

The only conceivable benefit of this prospective proposal would be either for tape recorder repair shop owners or for people who plan to corner the market on existing phonorecords.

You could be quite sure that, unless the encoding mechanism can be disabled, whoever buys a recorder on December 31, 1987 (if there are any on the shelves then) will have bought the last for quite some time. With tens of millions already in circulation, who will want a new one that can't record certain new material? People will buy new recorders with encoding mechanisms only if they know someone who can disable the mechanism.

The reaction of record buyers would be even stronger. Customers would boycott encoded material as a matter of principle, until the record companies break ranks and/or the law is changed. This proposal is reminiscent of movie studio attempts to change home video from essentially a rental market to a sale market--people simply won't stand for it.

In short, this proposal, in addition to being unfair to consumers, has the breathtaking potential to destroy the "hardware" and "software" markets simultaneously. We believe it is far better for these markets both to continue to grow in complementary fashion, and to continue to serve, rather than oppress, consumers.

Mr. Ferris:

Your written testimony notes that enactment of S. 1739 would be in "direct contravention of the Supreme Court holding in Sony v. Universal City Studios." In fact, doesn't that case stand for the proposition that it is up to Congress, through the legislative process, to adapt to new technology by redefining the scope of contributory infringement? Isn't that just what this bill tries to do? In what respect does this bill contravene Sony?

Sony v. Universal

Anyone who thinks the Sony decision was a simple invitation to the Congress, rather than a fundamental analysis and application of the doctrine of contributory infringement to copyright, is, in my opinion, grossly mistaken. What the Sony decision demonstrates is that there is not, and cannot be, any reasoned legal doctrine to support the enactment of royalty tax legislation.

Essentially, what the Supreme Court held is that it cannot be contributory infringement for a manufacturer to sell a product that, in addition to its allegedly infringing use, has substantial noninfringing uses. The finding that time shifting is fair use, and therefore noninfringing, provided enough evidence for five Justices to reverse the Ninth Circuit--the others would have remanded for further fact-finding. The substantial non-infringing uses of audio blank tape and recorders, however, are manifest.

While of course the Congress is free to make reasonable or unreasonable laws, on reflection one sees that, with respect to contributory infringement, the Court made a correct and essential determination. Otherwise, owners of patents, copyrights, and trademarks would constantly be seeking levies on manufacturers of allegedly infringing products with substantial noninfringing uses. Inevitably, hardware and software proprietors would be seeking such levies on each other, because their products are complementary.

The Sony decision affirms that plain paper may be sold, even though there are "plain paper copiers." It erects a formidable burden of proof for those who would tamper with the basic doctrine that manufacturers of products with substantial noninfringing uses ought to be left alone.

Nothing about home taping or technology, apart from record companies' desire for a windfall, requires that the doctrine of contributory infringement undergo surgery. The evidence of uses that do not implicate copyright, that implicate but do not damage copyright, or are beneficial to copyright holders, is simply overwhelming. To paint new technology as a bogeyman is to ignore the role it played in the birth and expansion of the recording industry, and to ignore recent history. The basic argument that brought RIAA to the legislative table--that home taping was responsible for the industry's problems in 1982--has by now been thoroughly discredited.[1] There is simply nothing, beyond the shibboleth about technology, to suggest that the Supreme Court was wrong, or that Sony principles should not be applied to audio home recording.

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[1] See p. 324, Widdows & McHugh, Taxing Purchases of Home Tape Recorders and Supplies to Compensate for Copyright Infringements: An Econometric Analysis of the Role of Economic and Demographic Factors, 18 J. Consumer Aff. 317 (1984)(attached).

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RICHARD WIDDOWS AND RICHARD J. McHUGH

Taxing Purchases of Home Tape Recorders and Supplies to Compensate for Copyright Infringements: An Econometric Analysis of the Role of Economic and Demographic Factors

Faced with a sharp decline in sales in the early 1980's, the music industry looked for an explanation which could be converted into windfall gains for itself. The explanation proposed by the industry was increased home taping of prerecorded music. Through the introduction of federal legislation, the industry hoped to realize gains at the expense of the consumer of home taping equipment and media. The analysis presented here indicates that the independent effect of taping on prerecorded music sales may not have been as high as the recording industry has claimed, so that consumers may end up paying more than their fair share toward the windfall.

The U.S. Senate hearings held in 1981 and 1982 on S 1758, a bill to exempt the private, noncommercial recording of copyrighted works on video recorders from copyright infringement, were originally inspired by the need to protect the consumer's right to tape signals entering the home for replay at a later time. The bill was introduced in response to suits brought by Universal Studios and Walt Disney Productions against Sony Corporation of America, on the grounds that video recorders produced by Sony and others infringed upon their copyright material. Video cassette recorders represent a technological innovation which had stretched the limits of the Copyright Act. S 1758 was an attempt to resolve the issue so that individuals could record copyrighted material without breaking the law.

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ISSUES INVOLVED IN THE COPYRIGHT OF PRERECORDED MUSIC

While the substantive issue at stake focused on the copyright and consumers rights, the rights of owners of copyrights were involved too. Furthermore, this latter interest went beyond video cassettes to home taping of audio material. S 1758 emerged at a time when the music industry was in the first throes of a slump from which it has still only partially recovered. Sales of prerecorded music had plummetted since the late 1970's, and layoffs had commenced among factories producing prerecorded music. The search for explanations for the slump had commenced, and home taping was heavily implicated. S 1758 soon represented to the recording industry a means of offsetting its losses, by mandating a surcharge on home taping.

The Mathias Amendment

To protect artists' rights, the recording industry proposed that a special "tax" be placed on recorders and/or blank tapes. Proceeds from the tax would be distributed to copyright holders. The tax was not part of the original S 1758; indeed Senator DeConcini, an advocate of the bill, spoke against it in his opening statements [5, p. 2]. By the time of the second session of the hearings, however, it had emerged as Amendment 1333, the so-called "Mathias Amendment."

The Mathias Amendment provided for a compulsory license on importers and manufacturers of equipment and media which could be used for taping at home, and specifically referred to audio as well as video recordings. The license fee would be the special "tax"; proceeds would be distributed by the Copyright Royalty Tribunal to applicant copyright owners. The means of calculating fees were not specified; the only provision was for "fair compensation." Mathias' stated aim was to protect the creative artist. It emerged in the hearings, though, that the music industry saw the amendment in different terms—as a protector of the recording industry.

The Music Industry Viewpoint and the Electronics Industry Rejoinder

The music industry was represented in the hearings principally by the Recording Industry Association of America (RIAA). The RIAA drew on four home taping surveys and an economic study based on the survey results, conducted by Greenspan-Townsend [5, pp.

921-937]. The latter claimed that potential sales of prerecorded music were being lost to home taping, and an estimate of $900 million was presented for 1981 alone. Further, prices of prerecorded music were lower by 18 percent than what they would have been had the competition of home taping not been present. The RIAA strongly endorsed the Mathias Amendment as a means of compensating for lost sales.

The view that the music industry's troubles stemmed from the substitution of home taping for purchase of prerecorded music was challenged by the Electronics Industry Association (EIA). As evidence, the EIA pointed out that audio hardware sales were down as well as software sales, and claimed that the demand for music was in recession. The EIA cited several reasons for this decline, including the general recession in the economy, changes in demographics, low quality of discs and prerecorded tapes, piracy, and the competitive consumer expenditure on video games [5, p. 641]. Hard empirical data were not, however, forthcoming on any of these points, a fact which enabled the RIAA to have several last words on the subject [5, p. 659].

The Greenspan-Townsend Study

At the time of this writing, the issue of the tax is in abeyance, but it is by no means dead.[1] In January 1983, Mathias introduced it in the Senate, in the form of the "Home Recording Act" (S.31) of 1983. This bill incorporates the ideas encompassed by the Mathias Amendment, as described earlier [4]. Greenspan-Townsend's evidence remains the only serious estimate of sales loss due to home taping, and it is likely that it would serve as the basis for calculating a surcharge on home taping equipment or media, should one be approved. Such a calculation, we will argue, would in effect incorporate into the surcharge the dynamic effects of adverse economic and demographic change on sales of prerecorded music. This would be unjust to consumers. Any surcharge should be calculated independently of the effects of economic and demographic change. Such effects would be

[1] In January of 1984 the U.S. Supreme Court approved home taping of TV shows by a 5-4 majority. The Supreme Court did not specifically address the recording industry, however. The recording industry is still pressing for action by Congress along the lines indicated.

(and are being) reversed as the economy improves. A surcharge based on Greenspan-Townsend data would be unnecessarily high, and the recording industry would receive an artificial subsidy from consumers.

SOCIO-ECONOMIC ANALYSIS

Despite the RIAA position and Greenspan-Townsend's evidence, the EIA position that the state of the economy and certain other changes have impacted significantly on the demand for prerecorded music has not been refuted. Greenspan-Townsend's methodology consisted of using cross-sectional survey data on home taping to derive a dollar equivalent for retail loss from home taping. This procedure effectively "freezes" any dynamic influence on sales other than home taping, making the observed linkage between home taping and sales a molar causal connection [6]. It is our contention that economic and demographic change represents a mediating mechanism that is involved in the relationship, a mechanism that should be measured separately in a functional equation as a relevant cause of sales change.

Such an equation has been put forward in an econometric analysis of prerecorded music industry by Belinfante and Johnson [1]. The functional equation they used to estimate sales of records and tapes is as follows:

$$Q = f(Q_{-1}, G, P)$$

where Q is quantity sold, G is real gross national product, and P is real price of records and tapes. The equation was estimated by log-linear least squares regression analysis for the period 1969-80 using annual data. The price coefficient proved insignificant and was subsequently dropped.[3] The model which remained provided only limited insight into the industry, and the few other economic studies of the industry which are available did not offer more.

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[3] While it would have been desirable to include a price variable for this study, construction of a meaningful series on prices for the prerecorded music industry proved difficult, and the series used performed poorly in test runs. It was accordingly eliminated from the final equation in this paper. It should be mentioned that Belinfante and Davis [2] also found price to be insignificant in their equation.

METHODOLOGY

The main shortcoming of the Belinfante and Johnson model as far as the present discussion is concerned is that the independent variables do not incorporate interaction among demographic change, the state of the economy, and the sales of prerecorded music. In the analysis to be presented here, total prerecorded music sales are related to household personal income and the employment level of an appropriate age cohort of the population.[3] The equation developed for estimating music sales is relatively simple; more complex specifications did not improve the explanatory power of the model significantly, while creating multicollinearity problems.

The general form of the equation estimated here is:

$$S = a + bY + cE + dD + e$$

where S is total sales of prerecorded music, Y is the level of personal income of the U.S. population, E is the employment rate of persons between 16 and 24 years of age, and D is the dummy variable for the years 1977 and 1978.[4] Data on sales and income were adjusted by the GNP deflator for personal consumption expenditure.

The years 1977 and 1978 (the "disco" years) were extraordinarily good for the recording industry, with real sales up by 25 percent over the annual average of the previous five years. Simple modeling without dummy variables for these years might statistically, and perhaps spuriously, attribute explanatory power to any of the variables which changed over these years. The dummy variable controls for this impact and can perhaps be interpreted as a shift variable for those years.

The data for total prerecorded music sales were obtained from RIAA press releases. Employment data are from the Bureau of

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[3] In a fully-specified model, it would be desirable to include either sales or relative price of blank tapes as a variable in the analysis. This was not possible due to lack of adequate data.

[4] The 16-24 age cohort group proved to be the most effective one in forecasting recent change. Industry sources have argued that a broader age group is relevant to explaining total music sales. Recently, attention has reverted to this young group as being the driving force behind sales change, possibly because it has been the group most influenced by video promotion of recordings. In our analysis, the broader age cohorts did not perform as well as the 16-24 group in explaining variation in sales. Including age cohorts as separate variables—16-19, 20-24, 25-30, and so on—created collinearity problems.

TABLE 1
Relationship Between Economic and Demographic Variables and Prerecorded Music Sales: 1956-81

	I	II	III	IV	V
Intercept	−4.66 (3.63)	0.65 (4.31)	−5.37 (3.62)	−4.55	−2.54
Personal Income	0.71** (0.33)	1.37** (0.44)	0.69** (0.33)	0.85* (0.38)	1.01** (0.19)
Employment 16-24	1.93** (0.80)	0.65 (0.91)	2.07** (0.80)	1.85** (0.96)	– –
Employment 16-24, males only	–	–	–	–	1.58** (0.59)
Dummy variable, 1977-1978	0.12 (0.19)	0.18 (0.59)	–	–	0.13 (0.10)
R square	0.939	0.977	0.935	0.965	0.941
DW	0.44	1.11	0.55	1.27	0.45
Rho	–	0.96	–	0.69	–

Note. Figures in parentheses are standard errors.
*Significant at the 5 percent level.
**Significant at the 1 percent level.

Labor Statistics; income and price data are from the Bureau of Economic Analysis *Survey of Current Business*.

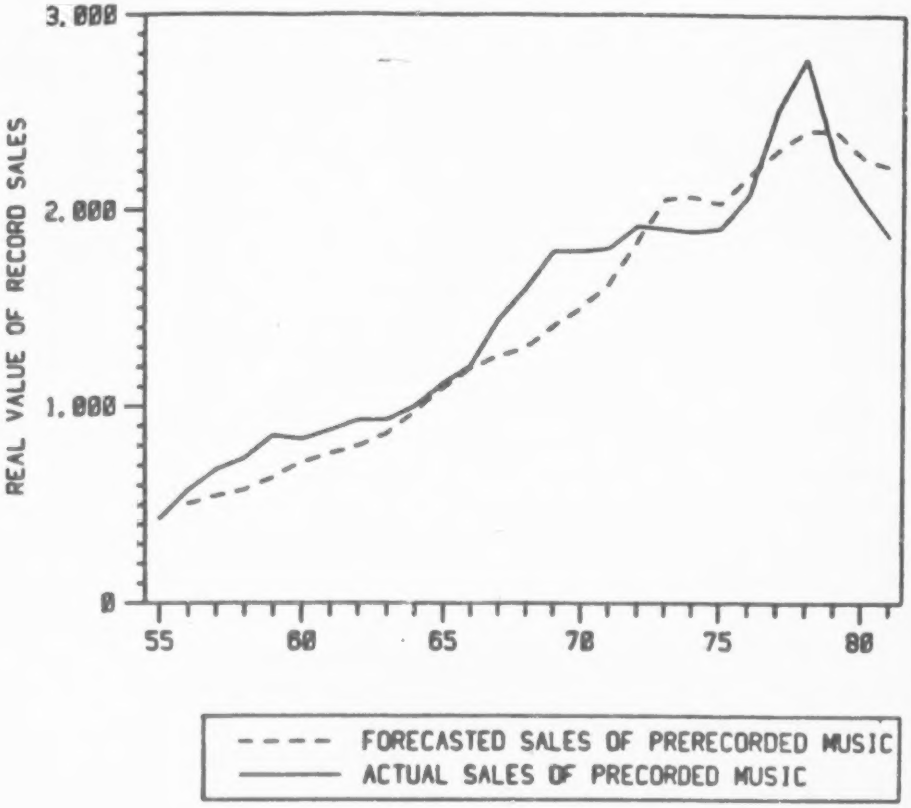
RESULTS

The equation was estimated by log-linear least squares regression analysis for the period 1956-81, using annual data. Results for five different specifications of the equation are shown in Table 1. In all specifications, signs of the coefficients of independent variables were as expected *a priori,* and a high proportion of the variation in the dependent variables was explained by the equation.

In specifications I and III, while the income and employment variables were highly significant, the low Durbin-Watson statistic indicated that serial correlation of the error terms might be a problem. Specifications II and IV therefore corrected for autocorrelation using the Hildreth-Lu procedure. The independent variables maintained their expected signs and explanatory power of the equation remained high.

In specifications I and II, the coefficients of the dummy variable, though of the correct sign, were not significantly different from zero.

FIGURE 1
Actual versus Predicted Record Sales



Specifications III and IV therefore excluded this variable. The significance level of the income and employment variables was not affected, and explanatory power of the equation remained high. This would question the need for the dummy for years 1977 and 1978.

In specification V, account was taken of a recording industry claim that males are disproportionately represented among the record-buying public. Employment in this specification was for males only. This substitution improved the explanatory power of the equation as compared to specification I.

To gauge the success of the model in tracking the turnarounds in industry performance, actual sales of prerecorded music were compared with sales as forecast by the model. The model did a very good job of tracking turnarounds. This can be seen from Figure 1, which shows the comparison using forecasts obtained from specification IV. Forecasts represent the impact purely of economic and demographic factors on sales of prerecorded music. As can be seen from Figure 1, these factors explain a large proportion of the decline of sales between 1978 and 1981. It is clear that even without surveys of individuals who tape record at home, one could have forecast a substantial decline of sales for that period.

As an instance, specification IV of Table 1 would have predicted a 29 percent sales decline from 1978 to 1981. Since the actual decline was 33 percent, it would seem that as much as 85 percent of the fall in sales over the 1978 to 1981 period was due to economic and demographic factors. Furthermore, in absolute terms, the residual in those years was smaller than in some earlier years when taping was thought to be much less pervasive. These findings cast serious doubts on the hypothesis that home taping was the cause of the collapse of the market in the early 1980's.

SUMMARY AND CONCLUSIONS

It is still possible that a surcharge will be placed on sales of home taping equipment and media, as a follow-on from the aforementioned Mathias Amendment. In effect this would represent a royalty tax placed on consumers. It will be justified by reference to artist and producer copyrights over prerecorded work. While there is some merit in the argument put forth by the owners of copyrights, our worry is that the amount of the surcharge may be derived from cross-sectional studies which do not assess the independent impact of economic and demographic change on sales.

Our attempt to control for economic and demographic effects on sales of prerecorded music in recent years through a dynamic economic model indicates that the independent effect of economic and demographic change is much greater than legislators have been led to believe. At the very least, this finding suggests that much more econometric analysis needs to be done before a "tax" is approved which would transfer millions of dollars from consumers to the recording industry.

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Mr. Ferris:

The brochures that the tape manufacturers distribute to their customers discuss measures like sensitivity, frequency response, drop out, dynamic range, and tape noise or bias. I presume that these measures are used to indicate the superior qualities of these tapes.

a- Is is not possible for the Copyright Royalty Tribunal to draw qualitative distinctions based on these measures and impose a royalty on tapes falling above a certain threshold?

b- What is your opinion of an amendment to S. 1739 that would impose a relatively high royalty on the highest quality tapes and leave the other tapes royalty free?

c- Do these brochures adequately inform consumers of the relative substitutability of audio recording tape?

Tape Classification

(a) Royalties on Tapes Above a "Certain Threshhold"

No, it is not possible for the CRT or anyone else to draw any sensible, meaningful or useful "threshold" for royalty tax purposes. Moreover, in light of the standard complaints about home taping, any such threshold would be backwards, even counter-productive, in effect.

Even if you assume that a "threshold" can be set by reference to the tape alone, reality sets in with the realization that, as Jack Battaglia of Memtek pointed out, all tape on the market today is as good or better than the tapes used in 98% of the prerecorded tapes marketed by record companies today. Although we have noted that many people tape because they are not satisfied with the quality of the prerecorded product (primarily due to recording speed rather than the tape), keep this in mind: these prerecorded tapes are now outselling phonorecords, which are of higher quality musically, by a margin of two-to-one.

So, where do you set your "threshold?" If you set it at or below specifications for tapes used in prerecorded cassettes your "exemption" is a fraud from the start--it covers nothing. If you set it just above the level of tapes used in prerecorded cassettes, you have missed your market and betrayed your original point. If your villains are "the kids" who supposedly buy a prerecorded tape and run off copies on inexpensive dual decks, they are already satisfied with the quality of the prerecorded tapes, so their behavior will not be influenced by a tax on higher quality tapes.[1] Also, their source material and recorders are sufficiently modest in specification that a higher "quality" tape would probably not sound any better.

Who are the people you would snare with a "threshold" royalty tax? They are those for whom taping is not a means to avoid purchase, but for whom taping provides an additional reason to purchase phonorecords. They seek to preserve their records or make them portable by the best means possible, at quality levels unavailable in a prerecorded product.[2] Therefore, to train an assault on these people, you must abandon the rationale relied upon by several Senators ("those kids!") and go after all home taping of music, for whatever purpose. If this subcommittee does not think it is proper for people to prefer to buy records, and to wish to preserve them, edit them, and make them portable, it should say so, rather than rely on a false rationale.

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[1] Of course, we reject the claim that this represents typical home taping. The Yankelovich survey established that of the tapes in the collections of the people surveyed, 51% were from records or prerecorded tapes that the taper had bought himself; 21% were from the radio and only 28% were from borrowed source material. (Table 8-3, page 54.) Moreover, after listening to tapes made from borrowed material or the radio, tapers very often would be impelled to buy the complete album from which a record was taped, or to by another album by that composer or artist. (Table 7-1, p. 48.)

[2] As Ed Foster has made clear, a prerecorded tape product, no matter how good the tape, cannot presently achieve the quality attained by recording on the recorder on which the tape will be played back. Foster statement, Oct. 30, 1985, p. 3.

Having said that the "threshold" idea is counter to the asserted rationale for legislation, we must also point out that it simply is not possible, as well. One of the important implications of the fact that the quality of a tape can only be judged by reference to the recorder with which it will be used is this: tape specifications are made with reference to a perfectly matched recorder, under ideal conditions. Indeed, recorders are designed for maximum performance when mated to a particular tape brand and formulation--usually undisclosed, and different for each recorder. Thus, the ideal mating between tape and recorder seldom occurs in the real world. This creates a large zone of uncertainty as to the actual performance of particular tapes under varied conditions. As a result, the specifications of the tape itself cannot reliably predict the level of performance. Any "threshold" set above the specifications for tape now used in prerecorded cassettes is meaningless.[3]

Given this fact, any threshold set at or above the "level" of tapes now used in prerecorded cassettes will be easily evaded. One can already envision the next Memorex advertising campaign, broken glass and all: "Is it taxed or is it untaxed? Only your pocketbook knows for sure!" If you are serious about both having exemptions and maintaining taxes on more than a tiny percentage of tape sales, the CRT will be shooting at a moving and amorphous target, generating only litigation and consternation for all concerned.

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[3] Again, this is not to say that prerecorded cassettes are equal in overall quality to all blank tape. Aside from the high speed at which they are recorded and the fact that they are not recorded on the recorders on which they will be played back, the prerecorded products may be inferior in housing, durability, and ease and accuracy of use.

As both Len Feldman (statement, p. 8) and Ed Foster (p. 10) have emphasized, the idea of "threshold" tape specifications will become simply useless when digital audio recording, which is already here in 8mm and soon will prevail for many or most audio applications, arrives in force. Foster stated the matter succinctly (p. 10);

> Once in digital form, an audio program can be stored on a wide variety of media because, in digital recording, the two most important criteria are storage capacity and access time. Concepts such as "distortion" and "signal-to-noise ratio" are determined by the devices used to convert the signal from analog to digital form and back again--the so-called A/D and D/A converters--not by the storage medium itself.

(b) Amendment Putting High Royalty on "Highest Quality Tapes"

In view of the discussion above, we think such an amendment, even though well-intentioned, would be irresponsible. First, it diverges from the alleged "kids" behavior that some Senators believe to be the objectionable element in home taping. Second, since the job of setting a "threshold" is one no drafter has yet tackled (for good reason), we assume it would be left to someone else, after the fact. This would be the worst and least responsible sort of legislation--the Congress claiming it has "done something" on the subject, leaving hapless bureaucrats to do the impossible and be roundly criticized for their inevitable failure. If Congress thinks a threshold is possible, it should draft the specifications and hold hearings on them.

(c) Brochures and "Substitutability"

Carol Foreman has received the same question and has explained why she finds the brochures neither misleading nor inconsistent with the testimony of Feldman and Foster.

Mr. Ferris:

Your testimony about the role for the CRT under this legislation was interesting. Let me say at the outset that I recognize that the CRT is not the only method for distributing royalties, and I would certainly welcome alternative suggestions. But your testimony raises some questions.

First, you assert that it has been shown "repeatedly and consistently" that the CRT lacks the "continuity, expertise and coherence" to distribute royalties. I know you are familiar with the D.C. Circuit's most recent pronouncement on this subject, because you cite the case (NAB v. CRT) in your testimony. Didn't the D.C. Circuit there conclude that the CRT was doing a reasonably good job of distributing funds from the cable compulsory license? Didn't it serve notice there that it would not be favorably disposed to further appeals from the CRT's decisions by what it referred to as "a highly litigious copyright-owner subculture"?

Second, you express doubt that the CRT could really handle the complex claims that would be made under this legislation. Is there really any qualitative difference in complexity between these claims and those the CRT now handles, involving myriads of copyright holders in programs transmitted over cable TV?

Third, you express pessimism over the likelihood that the claimants would voluntarily resolve their differences. Doesn't recent experience show that most claims before the CRT are resolved by the parties, and that this settlement process is being used more frequently as time goes on?

Finally, can you suggest an alternative procedure for distributing the royalties?

Copyright Royalty Tribunal

A. The Workings of CRT

First, with respect to the distribution mechanism

by which the proceeds from any royalty tax would be distributed, and, in particular, the Copyright Royalty Tribunal ("CRT"), the consensus of judicial and legislative opinion is that the CRT has performed its tasks woefully.

Reviewing National Association of Broadcasters v. CRT, 722 F.2d 922 (D.C. Cir. 1985), and other judicial decisions reviewing CRT proceedings, it is clear that the courts have concluded that the Tribunal has done anything but a stellar job, albeit one that passes judicial muster. The courts have not ever concluded that the CRT was doing a reasonably good job.[1]

As noted in my testimony, both former CRT Chairman Clarence L. James, Jr. and Jack Valenti of the Motion Picture Association of American have called for abolition of the CRT. Many, including former Chairman James, have pointed to its inefficiency and incompetence. See, e.g., Copyright Office/Copyright Royalty Tribunal: Hearing Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary, 98th Cong., 1st Ses. 99-108 (1983) (statements of Rep. Robert W. Kastenmeier and letter to Thomas C. Brennan, Acting Chairman, CRT, from Rep. Kastenmeier (Jan. 7, 1983)).

As reported in the attached article from the May 13, 1985, Washington Post, Rep. Kastenmeier has stated that the "tribunal is in dire need of reform." Rep. Norman Y.

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[1] Repeatedly, the courts have focused on the CRT's inadequate resources and its failure to explain the reasons in support of its conclusions. See National Association of Broadcasters, 722 F.2d at 929 n.9 ("We cannot fail, however, to fault the Tribunal for its summary rejection of this evidence without setting forth its analysis with some specificity as to why the evidence was deemed lacking."); NCTA v. CRT, 689 F.2d 1077, 1091 (D.C. Cir. 1982) ("the Tribunal was not always explicit when it rejected evidence proffered by the parties and it left doubt in some instances whether a given decision resulted from a considered policy choice or an understanding of statutory authority.") Despite its failings, they defer to CRT determinations because Congress has conferred upon the Tribunal a large measure of discretion.

Mineta added that he did not know "whether we even need the tribunal." Two proposals, H.R. 2784 and H.R. 2752, both of which would essentially abolish the CRT, are pending in Congress.

Nevertheless, regardless of the judicial or legislative views on the competency of the CRT, the question for Congress in connection with S. 1739 is whether allowing the Tribunal to perform the sort of "rough justice" calculation that it has carried out in the past would serve the purposes of the copyright law. As set forth in my written statement, the history of prior CRT proceedings demonstrates the inevitability of delays in distributing the proceeds from a home taping tax. As noted in your letter, the NAB decision itself describes the copyright-owner "subculture" as "highly litigious." Moreover, given the private nature of home taping, it will be impossible to assess with any precision the works that are taped; indeed, only surrogate measures--retail sales, airplay, and surveys--will be available to measure the incidence of home taping.

Thus, the long lead times and the inherent imprecision in the process ensure that there will be virtually nothing but the grossest sort of correlation between the revenues received from a royalty tax pool and the creative effort that is being "compensated" by the levy.

B. Complexity of Claims

Second, there is no doubt but that the claims that the CRT would sort out under S. 1739 are significantly more difficult than those that it now handles. Of course, as discussed above, even if the claims were as "simple" as those arising under the cable compulsory license, it is clear that the purposes underlying the copyright law would not be served by the kind of decisionmaking that has characterized disbursements of cable fees.

There are several reasons, however, why the procedure delegated to the CRT under S. 1739 is likely to be more complex by several degrees than the tasks that it has carried out in the past. First, whereas there is a relatively finite number of cable retransmissions and of programs that are retransmitted by cable systems, there are hundreds of thousands of pieces of copyrighted musical works and sound recordings. But, unlike the cable copyright scheme, where actual retransmissions can be monitored and their volume ascertained, it will be impossible (if not constitutionally questionable) for the CRT to measure which and how much of particular works are being taped in American homes.

C. Improbability of Claimant Settlements

History has shown that claimant settlements of proceedings before the CRT are infrequent. The fact that there has been a petition for review of virtually every such proceeding is demonstrable evidence that that is the case. Although the Copyright Act contemplates that claimant settlements are possible (as does S. 1739), in the words of the NAB decision, "in each of the first five distributions to date a controversy has emerged requiring CRT resolution" and "four of those five distributions have been appealed to this court." 772 F.2d at 926. The enormous complexity of any proceeding involving royalties from a home taping tax, makes it extraordinarily unlikely that settlements will be any more likely than in the cable area, especially given what is generally seen as "a highly litigious copyright-owner subculture." Id. at 940.

Moreover, although both the Copyright Act and S. 1739 encourage settlements, whether such settlements actually promote the public good is entirely unclear. Indeed, settlements may become part and parcel of anticompetitive behavior. Despite the dangers of such behavior, S. 1739 confers an antitrust exemption on claimants for the purpose of receiving, and disbursing further, proceeds from the royalty pool. As Sen. Metzenbaum pointed out at the hearing on Oct. 30, 1985, there should be the most rigorous legislative scrutiny of whether such an exemption should be granted at all.

That settlements-cum-antitrust exemption are likely to contravene the public interest is amplified by the extraordinary concentration of the music business; six record companies control over 80% of the market. The dangers in such a highly concentrated industry are manifest. For example, under the umbrella protection of the exemption, record companies could agree on how to divide the royalty proceeds that they might jointly receive through the Recording Industry Association of America, Inc.; such collaboration could effectively deprive creative artists of any contractual leverage in negotiating agreements to share in the home taping fund.

D. Alternative Procedure

Because the idea of a royalty tax is fundamentally flawed--it is simply preposterous to submit that all home taping is wrong and that copyright owners should be compensated therefore--there should be no mechanism for distributing royalties. We believe, however, that parties arguing that the copyright laws are being infringed have ample redress in the federal courts, historically the proper place for adjudicating interests between private parties.

In this connection, we note that assigning such tasks to the CRT raises not insubstantial constitutional questions. Recent Supreme Court decisions suggest that the process of allocating private interests, such as copyrights, between parties may not be undertaken by entities created by Congress pursuant to its Article I powers but is a function within the exclusive province of Article III courts. See

Thomas v. *Union Carbide Agricultural Prods., Co.*, 105 S. Ct. 3325 (1985); *Northern Pipeline Construction Co.* v. *Marathon Pipe Line Co.*, 102 S. Ct. 2858 (1982). Therefore, Congress should be especially wary of delegating the task of allocating well-established rights to an Article I tribunal such as the CRT.

[From the Washington Post, May 13, 1985]

SURVIVAL OF COPYRIGHT ROYALTY PANEL THREATENED

CONTROVERSIAL CHAIRMAN'S RESIGNATION MAY LEAVE TRIBUNAL UNABLE TO FUNCTION LEGALLY

(By Keith B. Richburg)

The Copyright Royalty Tribunal is in shambles.

Its chairman, Marianne Mele Hall, resigned under White House pressure last week after disclosures that she helped write a book attached as racist and insulting to blacks. The five-member tribunal now has only two members—and may not be able, legally, to conduct business—at a time when some key cases are scheduled for review, including one brought by media magnate Ted Turner.

More than $70 million in 1983 royalty fees is waiting to be disbursed. The tribunal—with a fiscal 1985 budget of $700,000—has never had a staff economist or accountant and only recently hired a staff lawyer. It has come to be seen as a dumping ground for well-connected political appointees, who often lack experience in the field.

These mounting problems have led supporters and critics to question whether the nine-year-old panel can, or should, survive.

"The tribunal is in dire need of reform," said Rep. Robert W. Kastenmeier (D-Wis), a longtime critic. "I do not know whether the agency is broken beyond repair."

Rep. Norman Y. Mineta (D–Calif.), at a news conference called because of the Hall episode, went a step further: "I don't know in this day and age whether we ever need the tribunal."

The tribunal was created by the Copyright Act of 1976, which was designed to give the owners of copyrighted movies and television shows some protection against cable television operators, who could snatch distant signals from the airwaves for retransmission.

The tribunal was supposed to set the fees cable operators would pay to retransmit distant signals. It was also to divise a formula for redistributing that money among the owners of the copyrighted material.

But from the start, the tribunal had problems.

First, as Washington copyright lawyer Bill Patry said, "The CRT was told to set new rates, but there's nothing in the statute to tell them what the right rate should be . . . They had to deal with some complex legal issues, with very little statutory guidance."

The commissioners also were hampered by their lack of expertise. Only the panel's first chairman, Thomas C. Brennan, former counsel to the Senate Judiciary Subcommittee on Patents, Copyrights and Trademarks, had any real experience in copyright law.

"The Carter administration did a number on us," said Bruce Lehman, a lawyer who was counsel to the House committee that wrote the copyright law. "It was viewed by the Carter administration as a resting place for people who had been well-connected in the campaign. We've been on a downhill slide since then."

The Hall episode underscored the CRT's reputation as a political resting place or, as Sen. Charles McC. Mathias Jr. (R.-Md.) once called it, "a useful place to put some otherwise embarrassing applications for jobs." Hall, 34, a lawyer who once had been fired from a job at National Savings & Trust Bank here for "insubordination," told a House panel that she had never practiced copyright law and that her only relevant experience was a summer internship in the Copyright Office.

Hall was, however, associated with a variety of conservative groups—particularly High Frontier Inc., led by retired Lt. Gen. Daniel O. Graham, whose study into space-based antinuclear technology became the basis for the Reagan administration's "Star Wars" missile defense plan.

The other two commissioners, Edward Ray and Mario Aguero, are from the entertainment industry. Ray was a California state co-chairman for Republican Black Voters for Reagan-Bush in the 1980 presidential campaign. He also was an adviser to the Black Republican Council during the 1984 campaign.

Aguero, a Cuban immigrant, founded a company in this country that dubs Spanish soundtracks onto American movies. He has served as public relations chairman for the Republican National Hispanic Assembly.

Only last week the White House nominated another well-connected Republican to the commission—Rose Marie Monk, a personal aide to Reagan's longtime political adviser Lyn Nofziger. Monk said she has no copyright experience.

Usually, members of federal regulatory boards can turn to their professional staff of accountants and lawyers. But since the start, the CRT commissioners have worked with only their secretaries and pocket calculators. The tribunal initially was given about $500,000 for staff, which it never used.

"You don't turn back hundreds of thousands of dollars to the Treasury," Lehman said. "Then the CRT became a little bit of a political football, a little bit of a whipping boy."

Since then, the CRT's decisions have come under repeated attack in the courts. Cable television operators were particularly incensed by the last rate that the tribunal set, requiring to pay 3.75 percent of their profits to copyright owners, a figure they felt was too high. The rate, however, has been upheld by the U.S. Court of Appeals here.

Some had hoped that Hall might be able to rejuvenate the agency. In her short time as chairman, she had hired the tribunal's first general counsel.

Now, with all the new doubts about the tribunal, the question becomes: if it doesn't set the copyright rates and distribute the fees, who should?

"I am looking at the Copyright Royalty Tribunal in terms of reforms," Kastenmeier said in an interview. "I think that . . . there may be some interest [in Congress] in whether some other type of entity can handle the same responsibility." Most often mentioned, he said, are the federal courts or a new Commerce Department office.

The motion picture industry, which holds many of the copyrights in question, favors direct negotiations between copyright holders and cable television operators, said Fritz Attaway, vice president and counsel for the Motion Picture Association of America Inc.

But that raises the question of who would do the negotiating. A single broadcast, often can involve hundreds of copyright holders.

Mr. Ferris:

Please provide a description of the Audio Recording Rights Coalition including a complete list of all of its members.

The Audio Recording Rights Coalition (ARRC) is comprised of manufacturers, distributors, retailers, and consumers of audio recording equipment and blank tape.

Many prominent trade associations and consumer groups are members of the ARRC, including:

American Council of the Blind
Washington, D.C.

American Retail Federation
Washington, D.C.

Association of General Merchandising Chains
Washington, D.C.

Car Audio Specialists Association
Washington, D.C.

Consumer Recording Rights Committee
Washington, D.C.

Electronic Industries Association
Washington, D.C.

International Society of Certified Electronic Technicians
Fort Worth, TX

National Association of Retail Dealers of America
Chicago, IL

National Retail Merchants Association
Washington, D.C.

National Association of Television and Electronics Services of America
Chicago, IL

National Electronic Sales and Service Dealers Association
Fort Worth, TX

The ARRC is also comprised of several companies, including:

Alpine Electronics Corporation of America

Ampex Corporation

BASF Systems Corporation

Curtis Mathes

Fuji Photo Film USA, Inc.

General Electric Company

Hitachi Sales Corporation of America

International Jensen Inc.

JBL Incorporated

JVC Company of America

Kenwood Electronics

Matsushita Electric Corporation of America
(Panasonic, Quasar)

Maxell Corporation of America

N.A.P. Consumer Electronics Corporation

NEC Home Electronics (U.S.A.) Inc.

Sears

Sanyo Manufacturing Corporation

Sony Corporation of America

Sansui Electronics Corporation

Tandy Corporation

TDK Electronics Corporation

3-M Company

TEAC Corporation of America

Toshiba America, Inc.

Yamaha Electronics Corporation

Zenith Electronics Corporation

RESPONSES OF CHARLES D. FERRIS TO QUESTIONS SUBMITTED BY SENATOR DECONCINI

Questions for the Audio Recording Rights Coalition/Mr. Ferris

1. **Let's assume that during the Thanksgiving break while I am out in Arizona, I hear a new record that I like very much.** I like it so much that I decide several of my friends back in Washington would like it to and so I decide to give it to them for Christmas. But then I discover that the record costs $7.99 a piece. I decide that instead of buying 8 records at approximately $64, I'll just buy one for myself and 8 blank tapes to record the record. Assuming the tapes cost $3.00 a piece I've saved about $40.

Is this fair?

Who loses and who gains, besides myself, in this situation?

Is there a solution to this problem short of adding a penny a minute costs for each blank tape and a 25% surcharge on my recording machine?

2. I understand that the new technology will be 8 millimeter tape on which both audio and video will be recorded. Would this bill apply to the new 8 millimeter tape? Wouldn't this application mean that we were adding a royalty to video recording also? How many minutes of audio recording can be done on these 8 millimeter tapes? Under S. 1739 what would be the total royalty on this kind of tape? What would be the probable total cast of the tape both with and without the royalty?

1. The overall "fairness" of the practice you described depends on several factors. The important issue, however, is that the answer is not cut and dried. Home taping is far more complicated than the proposition that home taping equals displaced sales. Indeed, the recording

industry may very well actually gain from situation you have described.

To begin, however, I would like to stress that the practice of taping a record and giving away copies is rare. In other words, the practice you describe is completely atypical. Far and away, the prevalent practice is for home tapers to tape records or tapes in their collections for portability (to play on car stereos, on "Walkman"-type personal stereos, or in portable "boomboxes"), to preserve prerecorded music, or for selection taping--making composite tapes of favorite album cuts. People tape records and prerecorded tapes in their own collections and keep them.

The survey prepared for the Audio Recording Rights Coalition by Yankelovich, Skelly and White, Inc., entitled "Why Americans Tape: A Survey of Home Audio Taping In the United States," found that over half of all home music tapes are made from music in a taper's own collection. This is music that has been bought and paid for. Surveys commissioned by the recording industry confirm that this is the prevalent practice. See, e.g., CBS Records Market Research, "Blank Tape Buyers; Their Attitudes and Impact on Pre-Recorded Music Sales" 12 (Fall 1980); Roper Organization, Inc., "A Study On Tape Recording Practices Among The General Public" 6 (June 1979)("Roper Survey")(tapers'' own record and tape collections are "the largest single source" of home recordings).

Second, the home taping episode you have described has a much broader impact than that you simply appear to have saved $40. Initially, would you actually have bought eight copies of the record at $8.00 apiece? If not, you have not deprived the record company of any money at all--because you would not have purchased all the records in the first place.

Moreover, although you may have saved money, the record companies may benefit in the long term. More precisely, the practice you have described highlights how home taping actually stimulates sales of prerecorded music. Your friends might not have been exposed to the music had you not given it to them. Thus, if your friends liked the music as much as you did, they are likely to be inclined to buy other records by the same artist or records containing similar music.[1] Who benefits, then? Not just you and your friends, but the record company's bottom line.

Even assuming that the practice you have described is common, which it is not, or is economically harmful to the industry, as to which the overall gains and losses are much more complex than the industry portrays them, the "remedy" of taxing tape and recorders is wrong-headed. First, a tax on blank tape and recorders would tax nearly one-half the uses of those products that have nothing to do with prerecorded music. Is this fair? Who loses and who gains?

Moreover, even for those who tape prerecorded music, the "remedy" is irremediably defective because it taxes completely legitimate uses; people recording music in their own collection for portability, convenience, and selection taping. To tax these uses is to buy the argument of the recording industry that people should be forced to listen to music that they have purchased only in their living rooms, but not in their cars, at the office, or on the beach. People should not be forced to buy multiple copies of the same work--whether it be a record or a book--when they want to expand the scope of the area in which they enjoy it. Yet, that is precisely what the recording industry wants people to do!

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[1] The Yankelovich Survey found, for example, that home taping of borrowed records has introduced two out of three tapers (64%) to musical artists or composers whom they discover that they like, and well over half (57%) have been prompted to buy records or prerecorded tapes after taping an artist's work. Yankelovich Survey at 16, 45-48.

In sum, we reject the notion that there is any "problem" that requires any "solution." The taping tax "solution," however, is wholly unwarranted because it would burden the millions of consumers who engage in perfectly legitimate activities. The patent unfairness of S. 1739 or any other royalty tax proposal unquestionably means that that the "remedy" is far more devastating to the creative community, and the American public, than any alleged injuries from home taping practices.

2. Audio Royalty on 8mm "Video" Tape

You are correct--the new "8mm" format is widely regarded as the "next" video recorder format, and also was specifically designed for digital audio recording. Several manufacturers have machines on the market today that, at the push of a button, use their "video" tape to record audio signals "without accompanying visual images." As both Feldman (pp. 3-4) and Foster [pp. 7-8) have pointed out, this is true, as well, of existing Beta Hi-Fi and VHS Hi-Fi "video" recorders. In all cases, "hi fidelity" audio recordings can be made on the standard ("lowest") grade of video tape, at the slowest speeds.

As Feldman pointed out (pp. 11-12), this means that S. 1739 would tax a standard T-120 VHS video tape at $3.60 (T-160 at $4.80)--as in the case of many audio tapes, this probably would double the wholesale price. As to 8mm, Feldman pointed out that several recorders now on the market, having 12 hour recording capability for audio, would cause their tapes to be taxed at $7.20. One recorder is capable of 24 hours, so perhaps all 8mm "video" tape would be taxed at $14.40! At present, these blank tapes cost about $8.

S. 1739 applies to these recorders and tapes because it defines an "audio recording" as an "aurally perceptible copy (without accompanying visual images)."

While several people have said that S. 1739 needs to be changed so as not to cover Beta Hi-Fi, VHS Hi-Fi, 8mm, and their accompanying tapes, we don't see how this can be done in any principled way that will apply to new products as well. Len Feldman discussed this problem in depth at pp. 4-7, as one of the reasons why he concluded (p. 11) that S. 1739 is "unfixable."

So yes, you would be adding a royalty to video recording also. Aside from the obvious unfairness of doing this, and the fact that the sponsors have said they don't wish to do this, there is a political implication as well. Will Hollywood sit by and watch record companies tax "video" products, and thereby amass a warchest to outbid them for new entertainment, communications, or real estate properties? Indeed, if S. 1739 makes legislative progress (in any form), the juggernaut for a "video" tax on recorders and blank tape--already idling on the sidelines--will certainly take the field.

[From USA Today, November 19, 1985]

KODAK DEVELOPS MEGADISK

(By John Hillkirk)

A picture is worth 1,000 words but a new Kodak product stores 1.44 million words.

The book-size floppy disk drive, one of three 5¼-inch drives Eastman Kodak Co. unveiled Monday for personal computers, can store 12 megabytes of information. (One megabyte equals 400 pages of double-spaced text.)

That's a dramatic leap over 1.6-megabyte drives.

"A 12-megabyte floppy is something I'd like to see," said Jeff Stives of Compaq Computer Corp. (A Compaq drive stores up to 1.2 megabytes.)

Yet Kodak's latest thrust into electronics faces challenges.

The 12-megabyte drive won't be out until next summer. (A 6.6-megabyte model will debut in spring, and a 3.3-megabyte drive is available now for $285. Diskettes for the drives are available now, from Verbatim Corp, a Kodak unit.)

The Japanese, who dominate this business, aren't standing still. Fujitsu Ltd. and Toshiba Corp. already have displayed prototypes of 5- to 10-megabyte drives.

Said George Colony, president of Forrester Research Inc., "It's heartening to see an American company doing this, but they're not jumping ahead of everyone else."

Kodak must pitch the drives to Compaq, IBM Corp. and Apple Computer Inc., which have long-standing deals with other suppliers. (Apple buys 3½-inch drives from Sony Corp.) Notes Michael W. Ellmann of Wertheim & Co. Inc., "Kodak can't control this market like it does photography."

Computer makers will demand a second source for high-capacity drives. "Big-time success will come only if other firms start making them," said James Porter of DISK/Trend, a research firm.

Senator MATHIAS. Mr. Battaglia.

STATEMENT OF JACK C. BATTAGLIA

Mr. BATTAGLIA. My name is Jack Battaglia, and I am the general manager of Memtek Products, a division of Tandy Corp. As a division of Tandy, we are part of $3 billion corporation engaged principally in the manufacture and sale of consumer electronics products. Tandy has almost 7,000 retail outlets nationwide through which it sells products from its over 30 manufacturing plants. Tandy employs over 27,000 people in the United States and last year had net sales of almost $3 billion.

Memtek manufactures and sells blank audio and video tape, accessories for audio and video players, rechargeable alkaline batteries, and computer floppy disks. Except for floppy disks, which are sold under the Memtek name, all of our products are sold under the Memorex trade name. Tandy is the leading supplier of blank tape to American consumers. All Memorex blank audio tape sold in the United States is manufactured here. Memtek has manufacturing plants in a number of States including Texas, California, and Illinois. Memorex tape, which is sold in over 35,000 retail outlets nationwide, is the heart of our business.

I am testifying here today because I am outraged that Congress would consider taxing my company and our millions of customers for the benefit of the big recording companies and superstar singers who today are making money hand over fist. At a time when the record companies are enjoying record profits, this legislation is unnecessary. Even if they were not doing so well, it is unfair to tax all blank tape when most blank tape is used for taping which has nothing to do with copyrighted music. Even people who use our tape to record music are not hurting the record companies because these people are the same ones buying all the record companies' products. In fact, I believe taping technology, which has made portable music a reality, is in large part responsible for the record profits currently enjoyed by the recording industry. Any tax on my company would be unfair, but this particular tax would almost double the price of some of our tape and would have a drastic effect on our business and customers. Moreover, the magnitude of the tax would likely distort future development of technology in this area which is moving toward the merger of audio and video formats. The effect and scope of this legislation are very broad and Congress must recognize that the repercussions could be great. The members of this subcommittee should also recognize that the exemptions, which purport to narrow the focus of the bill, are unworkable. As a result, this ill-conceived tax will end up applying to all blank tape and everyone who uses it.

THIS LEGISLATION IS UNNECESSARY

Before the Senate considers transferring hundreds of millions of dollars from one industry to another and taxing the consumer, this subcommittee ought to determine whether that industry needs the money. The recording industry just finished one of its best years ever. When I look at these record profits, I cannot believe that they are asking Congress for a bailout. Is there no end to greed? It seems to me that with those kinds of profits, they have more than enough money and their fear that consumers will be deprived of new music is unfounded. The record companies clearly are not hurting, but they see an opportunity and they are going for it. They are trying to take a kernel of an argument—that some people sometimes make copies of their records—and parlay that point into a windfall of hundreds of millions of dollars. Their whole line of argument, however, conveniently ignores how blank tape is really used.

BLANK TAPE DOES NOT HURT THE RECORD INDUSTRY

Most blank tape is not even used to tape prerecorded music. Audio tape is used by industrial users, such as record companies, to make prerecorded cassettes. It is used by institutional purchasers such as religious groups like the Mormon Church, which buys a tremendous number of tapes to spread their gospel and to educate their missionaries. And it is used by consumers. Memorex tapes are sold predominantly to consumers—as much as 90 percent of our blank tape is bought by consumers. These consumers include college students who tape class notes; legislators who tape meetings; musicians who tape their own music; and, to a small degree, audiophiles who tape prerecorded music. The majority of the taping done by these consumers, however, is not of prerecorded music, as a survey conducted by Yankelovich, Skelley & White has demonstrated.

Many of these consumers who do tape prerecorded music do so not to avoid buying records, but to get the best quality portable music possible. Consumers have never been able to buy high-quality prerecorded music in audio cassette form. The cassettes used by the recording studios to make prerecorded tapes are inferior to the audio cassettes we make. In fact, I would say the best prerecorded tape is no better than the bottom-of-the-line Memorex tape. Moreover, the prerecorded music is inferior to the music an audiophile can have by making a tape of a record or compact disc. This is so because a consumer can make his tape in real time; whereas, recording companies tape at speeds up to 64 times real time. In this mass production process, much of the music's quality is lost. Therefore, many of our customers who want music in a prerecorded tape format will buy both the record and our tape and make their own cassette rather than buy the industry's inferior cassette offering. Our tapes are also often used to make customized tapes using selections from several albums. By and large these albums are also owned by the consumer.

Home tapers tend to be audiophiles, the people who love music and are the biggest purchasers of the record companies' products. Whether they are making customized selections or just transferring their music onto cassettes, the reason these people tape is not to avoid purchasing an album, but because taping is the best, and sometimes only, way to get a quality cassette of a musical work. These consumers tape because they have a demand that is not being met by the recording companies. The recording companies, therefore, cannot claim they are losing sales of albums when they are not even selling what tapers want to buy.

I recognize that, during the last few years, the recording industry has begun to respond to the strong demand for prerecorded music in cassette form, and it has upgraded the quality of its prerecorded tapes. It still has a long way to go, but even the initial efforts have been rewarded with vastly higher sales of prerecorded tapes. In fact, thanks to the taping technology which allowed prerecorded music to become portable, the record industry is now selling twice as many cassettes as records. I expect that with continued improvement in the quality of prerecorded cassettes, the record industry will continue to expand their sales. And, if the record industry ever gets their act together and produces enough compact discs to meet an ever-growing demand, their sales could go through the roof.

One result of the record industry's success in meeting the demand for music in cassette form is that sales of blank cassettes over the last 3 years have been rather flat. This slowing of demand for blank cassettes confirms that much of home taping was done because music lovers had no other source for good portable music and that many former tapers are now buying the record companies' products. I should add that while sales of blank cassettes are not rising, uses for the blank cassettes other than for home taping of prerecorded music have been increasing. For example, we sell many more tapes today for telephone answering devices than ever before. This overall decreased demand for blank tapes for recording music certainly calls into question recording industry claims that home taping of their works is on the increase.

THIS LEGISLATION WILL HURT MEMOREX AND ITS CUSTOMERS

Congress should be aware that this legislation would have a serious effect on our business. First of all, this tax is not modest. According to the International Tape Association [ITA], a manufacturer's average unit sale price of audio tape—all lengths and types—is $1.05 per cassette. I figure that the average tax under the legislation will be 78 cents, assuming that 60 percent of tapes are 90 minutes long and 40 percent are 60 minutes long. The tax will therefore result in an increase in price of 74 percent. For some of our tape, the tax will almost double the price. My company will be unable to internalize such a large tax, or any other tax for that matter. Because my company survives on tight margins, we will have to pass this tax through to our customers. And, because our product is extremely price-elastic, this will in turn result in a significant decline in our sales of tapes and our revenue. I cannot predict how much our sales will decrease, but a loss of a substantial part of our business is very likely if this tax were to become law.

THIS LEGISLATION WILL INHIBIT TECHNOLOGY AND DEVELOPMENT

This tax is so substantial I believe it will have a serious effect on future technological development. Tape technology is moving in the direction of a merger of audio and video tape into one size and format. Because of this legislation, however, manufacturers will avoid the marriage of audio and video and try to keep video tape distinct from audio.

Video tape manufacturers may have already lost the opportunity to avoid the tax, however, because video tape may already be covered by this legislation. Hi fi VCR's produce such a high-quality audio sound that many audiophiles tape music on video tape. They can do this without taping any video image. Because the bill defines audio tape as any medium upon which can be fixed an aurally perceptible copy without accompanying visual images, I think all video tape may already be covered under the legislation.

THE EXEMPTIONS WILL NOT WORK

The possible coverage of video tape by the legislation is only one example of the bill being much broader than is apparent on its face. Another is the fact I previously mentioned: that the bill will apply to users and uses of audio tape and equipment which have nothing to do with prerecorded music. For example, a typical college student will purchase our tape to record a class. This student should not have to pay an additional 75 percent of the price for that tape to the recording companies. Of course, the sponsors of this bill will say that the student is exempt under the legislation, but I do not see how. I have read and reread the language which is supposed to exempt tape which will not be used for making audio recordings by individuals for private use. I have tried to figure out how these exemptions for noninfringing uses will work, and I have concluded they cannot work and they are only in the bill to make some possible opponents of the bill believe they will not be affected. It is clear to me that everyone who uses blank audio tape will have to pay this tax. If they are not to pay, how will they avoid the tax? How is a consumer supposed to get his money back after the manufacturer has paid it and passed it on? And how does a college student prove that the tape was used to record a lecture and not copy a record? And who does he have to prove this to?

The Copyright Royalty Tribunal may decide to put our retailers, who are closest to consumers of blank tape, in the position of having to work out a system to provide rebates and to figure out who is using the tape for what. But retailers do not have time to read materials on how to deal with such problems, and they certainly do not have time to take care of such problems. If forced to deal with these issues, many dealers might drop our product.

The other exemptions in the bill are no more realistic. For example, the Copyright Royalty Tribunal is supposed to exempt tape that is not suitable for making audio recordings on the basis of technical criteria. Whoever wrote this does not know anything about tape or does not care if any of it is ever exempted from the tax.

There are five grades of standard Memorex tape—we also offer three grades of microcassettes. In order of quality, our standard tapes are DB, MRXI, HBII, HBX, and CDX. Every one of these grades is suitable for making audio recordings.

There are no technical distinctions between the tapes which can be used to distinguish which tape is or is not tape suitable for recording music. Certainly someone using tape to record lectures is more likely to use our lowest quality tape, but that does not mean someone else could not use that same tape to record music.

In sum, these exemptions are no exemptions at all. Even if the drafters of the legislation could figure out how to limit the bill's very broad application, it still would be lousy law. Any tax on audio recorders and blank tape is unfair and unnecessary and I urge Congress to reject this legislation.

Senator **Mathias**. Mr. Feldman.

STATEMENT OF LEONARD FELDMAN

Mr. **Feldman**. Thank you.

Mr. Chairman and members of the subcommittee, my name is Leonard Feldman. I own a laboratory and consulting firm. I am a graduate electronic engineer and have been involved in the audio and video industries for more than 30 years both as an engineer and as a product evaluator and technical journalist. I have written seven books on audio subjects and currently my writing activities include that of senior editor of Audio magazine and technical editor of Video Review. I also serve as a representative from the United States to one of the technical committees dealing with audio standards of the International Electrotechnical Commission [IEC], a world's standards body. I am a member of the Institute of Electrical and Electronic Engineers [IEEE] as well as of the Audio Engineering Society [AES]. And for 6 years I have been a consultant to the Consumer Electronics Group of the Electronic Industries Association.

I am pleased to be here today to discuss S. 1739. I also feel a sense of responsibility, however, as a representative of the community that develops, tests, and writes about electronic equipment. This is so because I am convinced that, by enacting this bill, the Congress would be setting up a system to accomplish—and charging an administrative agency to implement—something that is technically not possible. The basic assumption on which this bill appears to be based is that, in the near future, it will be possible to distinguish whether recorders and media are designed primarily to record and store audio signals, or whether they will be used primarily for something else. This underlying assumption is simply not true. Also not true is the assumption that, even today, it is possible to distinguish among recorders and media designed and used to store music (prerecorded or otherwise) and those designed and used to store something else. The effects of this miscalculation on the public's use of these devices and media, and on the development of future products, is potentially disastrous. That is why I feel a heavy responsibility to explain, from a technical point of view, why this is so.

THE IDEA OF AN "AUDIO ONLY" BILL WITH RESPECT TO HOME RECORDING IS SIMPLY UNREALISTIC, IN LIGHT OF PRESENT PRODUCTS AND FUTURE TRENDS

Thirty years ago, when I became involved in the industry, the technology involved in recording sound on tape was relatively simple. The only tape recorders we had then were large open reel machines dedicated exclusively to sound recording. Since then, the technology has become far more complex and diverse. The cassette tape format, originally conceived by its inventors as a business dictating sound recording medium, has also become a medium for recording music—but it is also commonly used as a data storage device for computers and electronic typewriters, in labs for studying foreign languages, and in many, many other contexts.

The use of tape as an audio-recording medium gave rise to the hope that more complex video signals, or TV pictures, could also be stored on tape. That technology arrived for professional users in the early 1960's; by the mid-1970's home-video recorders became a reality, and today the home penetration of video cassette recorders, or VCR's, in the United States is fast approaching the 30-percent mark.

Clearly, a video recorder must also be able to record the audio or sound that goes along with the picture. All VCR's have this capability, so one might say that all video recorders are also audio recorders and all video tape is therefore audio tape. Technology, however, does not stop there. Today, popular products such as Beta Hi-Fi and VHS Hi-Fi VCR's enable average consumers to record state-of-the-art soundtracks on video tape. Technical measurements of the frequency response, dynamic range, and freedom from various forms of distortion usually exceed those obtained with "audio only" recorders available to consumers. Clearly, these machines would be taxed by S. 1739. Moreover, this excellent audio-only performance is available with all grades of video tape on the market—so S. 1739 would tax all video tape as well.

The merging of technologies has not stopped here. A new VCR format, popularly known as the 8-millimeter (8 mm) system, makes provision for recording stereo digital soundtracks to go along with the video pictures. Moreover, at the flick of a switch this new 8 mm recording medium becomes a digital audio-only recorder. Measured technically, audio recordings made with such recorders and video tape yield specifications that in several respects exceed those obtained with some "high quality" audio cassette recorders.

At the risk of setting your heads spinning (as do the heads in many of these recorders), I must tell you that, in my opinion, it will not be long before identical recording systems are commonly used to record not only audio and video, but computer data as well. By this I mean that a single piece of hardware and a single software product, unless the Government interferes, can and will combine to be the most common and efficient method for storing all three types of data. Explained in basic terms, the reason for this convergence should not be hard to understand. The efficiency of a recording system is basically a function of how economically it stores and retrieves data. When digital techniques are used, it makes no difference to the storage system whether the encoded signals—once they are decoded—produce TV pictures, sound waves from a harpsichord, or a data base. All that is important is that the medium have enough storage capacity to record the encoded information, and that the recorder and medium, in combination, retrieve it accurately, as quickly as it is needed. And even—as in the case of video—when digital techniques are not yet commonly used, a system with these characteristics is also likely to be an optimal system for storing and reproducing analog information.

I cannot predict for you, today, exactly what this common system will look like. Indeed, that is a major point of my testimony: This is a race that will go to the most economical and efficient system, unless you, through this legislation, impose an artificial handicap. The possibilities are many and diverse. One is a read-write optical recorder, similar to the compact disc and laser disc audio-video players that are already in widespread use, except that it could record as well. Already, even without any recording capability, computer data bases are being put on compact discs because of their huge storage capacity. And, for the same reason, many audio compact discs will soon be producing still video images, in the form of captions, lyrics, illustrations, or pictures that, to use the language of S. 1739, are "accompanying visual images." This capability is written into the basic format, is under active development, and has been widely demonstrated.

Perhaps the most efficient system will be based on magnetic tape recording. As production efficiencies bring costs down, a new generation of digital tape recorders could prove optimal for storing many kinds of audio, video, and computer information. All such information would be stored on identical formulations and compositions of tape, since, as I will explain soon, the properties of the tape matter little when digital techniques are used. For example, I have seen demonstrated a VCR with a built-in digital pcm processor that allows it to function as a VCR, or to record digital stereo audio on standard video tape, with no accompanying visual image. Again, ordinary video tape serves both purposes well.

The best combination might be one that uses magnetic discs of the sort commonly used now to store computer information. Already, there are commercial efforts underway to store music on floppy discs, of the sort used with personal computers, in competition with systems based on tape. This raises an interesting prospect that may have to be faced well before a common system is arrived at: Suppose the floppy disc chosen for a mass-market audio recorder system is identical to the one chosen for the next generation IBM PC. Do you tax it or do you not? If you do, you outrage, and rightly so, anyone who has bought or is about to buy the PC. If you do not, you give an enormous advantage to the disc-based product over the competing tape-based product, which seeks an identical market and is taxed only because it was not chosen for use with the most popular PC. (As I read S. 1739, the Copyright Royalty Tribunal would not have to face this question—both types of recorders and media would fall squarely within the definition of what is to be taxed, and neither could be excluded based on the rationale for any exemptions.)

S. 1739 IS FATALLY FLAWED, EVEN AS IT APPLIES TO EXISTING AUDIO PRODUCTS

It is not necessary to project into the future at all to discover fatal technical flaws in S. 1739. The bill purports to call for regulations to establish exemptions for tapes that are not suitable for high-quality musical programming. My own experience with tape testing convinces me that in the practical world of magnetic tape technology, this is simply an unrealistic proposal.

TAPE CANNOT BE CLASSIFIED ACCORDING TO USE

To begin with, any one of the four current generic types of tape may be used for any recording purpose. The generic categories of tapes now designated as Roman numerals I, II, III, and IV are simply assigned as an aid in identifying required recording parameters on a tape recorder, so that it will work properly with that particular generic type of tape. Within each generic category, the tape manufacturer may have any number of tape grades. Each grade is capable of making high-quality recordings of audio programs. Thus, a type I tape may easily make a better audio recording than a type II tape. Indeed, the quality of the tape can never be judged in isolation; it all depends on the design parameters of the recorder(s) with which the tape will be used. In my view, attempting to classify tapes in terms of their intended use is not only impractical; it is for all intents and purposes impossible.

What I have said about the prospects for classifying tape according to intended use is true even as matters stand now. But again looking to the near future, and at the technology that already exists in the laboratories of hardware and software makers, such categorization of tapes may be entirely meaningless in 1 or 2 years. The industry has already developed standards for dedicated home digital audio tape recorders. In the case of digital tape recording, the quality of the tape formulation has little to do with the quality of the recording that is made. In fact, one of the chief virtues of digital tape recording is that even tapes that would add very high levels of noise or tape hiss when used to make conventional analog audio recordings are perfectly suitable for use in a digital audio recording system. That being the case, I fail to see how any grading of tape types would serve to identify the uses to which those tapes ultimately will be put.

RECORDERS CANNOT BE CLASSIFIED ACCORDING TO USE

It is, and will continue to be, similarly artificial and destructive to attempt to classify recorders according to whether they will be used to store prerecorded music or to record or play something else. You do not need a technical background to be aware of the most basic argument against such an attempt—the fact that music is music. Thus, a recorder on which I might tape or play a recording of a Chopin piano sonata is one I would want to use also to record my practice on my own piano. Indeed, from a technical viewpoint, I should really state the proposition the other way around: The recorder on which I will wish to record my own piano practice will without doubt be one that I also consider suitable for recording and playing prerecorded music.

But even if you are prepared to be grossly unfair to the millions of amateur musicians in this country, you are still not much closer to having a fair and workable tax on recorders. My knowledge of technical trends leads me to conclude that it will be impossible to maintain any viable distinction between recorders used primarily for music and recorders used primarily for the spoken word. As to today's products, I call your attention to the common portable stereo cassette recorder/player, or "boom box." In the playback mode, these recorders are used both for music and for voice, although my trips to the beach tell me that playing back music predominates. These units almost all have built in microphones, however, as well as switches and jacks that permit users to make recordings from internal and external sources. The quality of such recordings often rivals those made on home recorders, and whether this is high fidelity depends on the price of each unit, the type of tape used, and your personal standards; yet, recordings through the built-in microphone, and many through external microphones, are likely to be, very often, of the spoken word.

In recent years, the "boom box" has been joined by its smaller and even more portable cousin, the Walkman-type player and recorder. Already, some of these hand held units are capable of performance in the recording mode that rivals home decks of similar price. I have such a unit. I have personally used it for in-the-field recordings of musical performances, with entirely satisfactory results. I also use it to record speeches, conferences, and panel discussions. In this context, its stereo capability is extremely helpful, as it permits me to better identify who is being recorded. In my opinion, hand held devices on which I would be pleased to record live or prerecorded music will soon be available to average consumers, and they will also be the most popular devices for recording the spoken word. The development of such popular all-purpose recorders will be denied to us only if one of those purposes is taxed.

THE INEVITABLE INEQUITIES AND DISTORTIONS

Let me just mention two more examples, from the trends I have discussed, to demonstrate why this bill is unfixable. How are you going to treat the hand held, multipurpose recorder that I have just described? As presently written, S. 1739 would tax it. Should the Copyright Royalty Tribunal create an exemption for this product? If it does not, the Tribunal will penalize all those who want to own the best and most flexible hand held recorders, including journalists, businessmen, educators, et cetera. It will create disincentives to the production of such recorders. If it does create an exemption, and limits the tax to nonportable decks, pretty soon most high quality decks will meet the definition of portable—it will be cheaper for the manufacturer to add the portability feature than to pay the tax. If the rationale for this legislation is to be maintained thereafter, the Tribunal would have to abolish the portability exemption and go back to taxing all recorders. This is why I firmly believe that an exemption that would actually work "as advertised" is simply not possible.

Returning to the video world, let us calculate the audio tax imposed by S. 1739 on existing video recorders and tape. On a Beta or VHS Hi-Fi recorder that sells for $500, the recorder tax would be $25. As to tape, a standard T-120 tape—the one most commonly sold by video retailers and others who sell video tape—would incur a tax, at the wholesale level, of $3.60. At retail, this would effectively double its purchase price. As to tapes used with several 8 mm video recorders that are already on the market, the tax would be $7.20.

What could the Tribunal do about this result? The tax rate is fixed by S. 1739. The choice would be to exempt a particular product or not to exempt it. This decision is arbitrary with respect to presently available products, and any outcome would distort future developments. And with respect to the products that will be available in the near future, there will be no basis at all for the Tribunal to decide: To tax or not to tax.

One might respond, of course, that the answer is to be sure to tax all new recorders and media—audio, video, computer—irrespective of the consequences. Mr. Chairman, based on 30 years' experience in this industry, I can tell you that this would not only be unnecessary; it would also be the greatest assault on technological innovation, and the benefits it offers society, since the Luddites. It would be unnecessary because every innovation I have witnessed, from color television through the video recorder to the compact disc, has proven ultimately to be strongly to the benefit of suppliers of programming. One might have thought that adding color to television would weaken the theatrical market for movies. And some people did think that the VCR would do this. Instead, the hugeness of the new markets that have been opened has become obvious to virtually everyone.

I refer to the Luddites because history has shown that you cannot suppress technological progress and you regulate it only when you must. The video recorder, the Walkman and the compact disc player—indeed, the microphone, the amplifier, and the phonorecord—were not free goods, willed to the entertainment industry. Nor were they invented by the entertainment industry. Opening new markets is expensive; shaping them is risky. It is a process that, in our society, we have left to free enterprise, rather than the hand of government. It is to this freedom of others to invest in new technology that I attribute much of the success of the recording industry, as well as other software proprietors. I see nothing on the horizon that I have surveyed for you today that threatens to diminish this success in any way—if the Government will only stay out of the picture.

Mr. Chairman, having reviewed the provisions of S. 1739, considered how it would operate on the products with which I have worked, and thought about ways in which the bill might be revised, here is my conclusion. This legislation is fundamentally at odds with the realities that govern home recording today, and will shape technology tomorrow. The very idea of having the Government officially distinguish audio recording devices and media from video devices and media is not just obsolescent; it is obsolete. The idea of a royalty tax on multipurpose recorders and media is distortive, even destructive, of socially beneficial technology. Even from the most narrow, short term perspective, attempting to apply this bill to the products available today will punish huge categories of users and harm the public, as potential developments of general application are forestalled by this tax. I urge you and the members of the subcommittee not to adopt this, or any tax.

Thank you for inviting me to appear today.

Senator MATHIAS. Thank you.

[Mr. Feldman's prepared statement follows:]

PREPARED STATEMENT OF LEONARD FELDMAN

Mr. Chairman and members of the Subcommittee, my name is Leonard Feldman. I own a laboratory and consulting firm. I am a graduate electronic engineer and have been involved in the audio and video industries for more than 30 years both as an engineer and as a product evaluator and technical journalist. I have written seven books on audio subjects and currently my writing activities include that of senior editor of Audio magazine and technical editor of Video Review. I also serve as a representative from the United States to one of the technical committees dealing with audio standards of the International Electrotechnical Commission ("IEC"), a world's standards body. I am a member of the Institute of Electrical and Electronic Engineers ("IEEE") as well as of the Audio Engineering Society ("AES"). And for 6 years I have been a consultant to the Consumer Electronics Group of the Electronic Industries Association.

I am pleased to be here today to discuss S. 1739. I also feel a sense of responsibility, however, as a representative of the community that develops, tests, and writes about electronic equipment. This is so because I am convinced that, by enacting this bill, the Congress would be setting up a system to accomplish -- and charging an administrative agency to implement -- something that is technically not possible. The basic assumption on which this bill appears to be based is that, in the near future, it will be possible to distinguish whether recorders and media are designed primarily to record and store "audio" signals, or whether they will be used primarily for something else. This underlying assumption is simply not true. Also not true is the assumption that, even today, it is possible to distinguish among recorders and media designed and used to store music (prerecorded or otherwise), and those designed and used to store something else. The effects of this miscalculation on the public's use of these devices and media, and on the development of future products, is potentially disastrous. That is why I feel a heavy responsibility to explain, from a technical point of view, why this is so.

The Idea of an "Audio Only" Bill With Respect to Home Recording Is Simply Unrealistic, In Light of Present Products and Future Trends.

Thirty years ago, when I became involved in the industry, the technology involved in recording sound on tape was relatively simple. The only tape recorders we had then were large open reel machines dedicated exclusively to sound recording. Since then, the technology has become far more complex and diverse. The cassette tape format, originally conceived by its inventors as a business dictating sound recording medium, has also become a medium for recording music-- but it is also commonly used as a data storage device for computers and electronic typewriters, in labs for studying foreign languages, and in many, many other contexts.

The use of tape as an audio recording medium gave rise to the hope that more complex video signals, or TV pictures, could also be stored on tape. That technology arrived for professional users in the early 1960s; by the mid-1970s home video recorders became a reality and today the home penetration of video cassette recorders, or VCRs, in the United States is fast approaching the 30 percent mark.

Clearly, a video recorder must also be able to record the audio or sound that goes along with the picture. All VCRs have this capability, so one might say that all video recorders are also audio recorders and all video tape is therefore audio tape. Technology, however, does not stop there. Today, popular products such as "Beta Hi-Fi" and "VHS Hi-Fi" VCR's enable average consumers to record "state of the art" sound tracks on video tape. Technical measurements of the frequency response, dynamic range, and freedom from various forms of distortion usually exceed those obtained with any "audio only" recorders available to consumers.[1] Clearly, these machines would be taxed by S. 1739. Moreover, this excellent audio-only performance is available with all grades of video tape on the market -- so S. 1739 would tax all video tape, as well.

The merging of technologies has not stopped here. A New VCR format, popularly known as the "eight millimeter" ("8mm") system, makes provision for recording stereo digital sound tracks to go along with the video pictures. Moreover, at the flick of a switch this new 8mm recording medium becomes a digital audio-only recorder. Measured technically, audio recordings made with such recorders and video tape yield specifications that in several respects exceed those obtained with some "high quality" audio cassette recorders.

At the risk of setting your heads spinning (as do the heads in many of these recorders), I must tell you that, in my opinion, it will not be long before identical recording systems are commonly used to record not only "audio" and "video," but computer data as well. By this I mean that a single piece of hardware and a single software product, unless the government interferes, can and will combine to be the most common and efficient method for storing all three types of data. Explained in basic terms, the reason for this convergence should not be hard to understand. The efficiency of a recording system is basically a function of how economically it stores and retrieves data. When digital techniques are used, it makes no difference to the storage system whether the encoded signals, once they are decoded, produce TV pictures, sound waves from a harpsichord, or a data base. All that is important is that the medium have enough storage capacity to record the encoded information, and that the recorder and medium, in combination, retrieve it accurately, as quickly as it is needed. And even (as in the case of video) when digital techniques are not yet commonly used, a system with these characteristics is also likely to be an optimal system for storing and reproducing analog information.[2]

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[1] These recorders are designed with jacks and function switches to facilitate connection to stereo systems, and most have special "audio only" switches that replace the video signal (needed for proper synchronization) with an electronic reference signal while eliminating any accompanying visual image.

I cannot predict for you, today, exactly what this common system will look like. Indeed, that is a major point of my testimony: this is a "race" that will go to the most economical and efficient system, unless you, through this legislation, impose an artificial handicap. The possibilities are many and diverse. One is a "read-write" optical recorder, similar to the "compact disc" and "laser disc" audio-video players that are already in widespread use, except that it could record as well. Already, even without any recording capability, computer data bases are being put on compact discs because of their huge storage capacity. And, for the same reason, many "audio" compact discs will soon be producing still video images, in the form of captions, lyrics, illustrations, or pictures that, to use the language of S. 1739, are "accompanying visual images." This capability is "written into" the basic format, is under active development, and has been widely demonstrated.

Perhaps the most efficient system will be based on magnetic tape recording. As production efficiencies bring costs down, a new generation of digital tape recorders could prove optimal for storing many kinds of audio, video, and computer information. All such information would be stored on identical formulations and compositions of tape, since, as I will explain soon, the properties of the tape matter little when digital techniques are used. For example, I have seen demonstrated a VCR with a built in digital pcm processor that allows it to function as a VCR, or to record digital stereo audio on standard video tape, with no accompanying visual image. Again, ordinary video tape serves both purposes well.[3]

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[2] For example, the 8mm format uses the same tape and recording facilities to store digital audio information and analog video information. The most important characteristic of the 8mm system is that it stores lots of information very compactly yet reproduces it as fast as it is needed.

The best combination might be one that uses magnetic discs of the sort commonly used now to store computer information. Already, there are commercial efforts under way to store music on floppy discs, of the sort used with personal computers, in competition with systems based on tape. This raises an interesting prospect that may have to be faced well before a common system is arrived at: Suppose the floppy disc chosen for a mass-market audio recorder system is identical to the one chosen for the next generation IBM PC. Do you tax it or don't you? If you do, you outrage, and rightly so, anyone who has bought or is about to buy the PC. If you don't, you give an enormous advantage to the disc-based product over the competing tape-based product, which seeks an identical market and is taxed only because it was not chosen for use with the most popular PC. (As I read S. 1739, the Copyright Royalty Tribunal would not have to face this question-- both types of recorders and media would fall squarely within the definition of what is to be taxed, and neither could be excluded based on the rationale for any exemptions.)

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3. As I read S. 1739, an ordinary (non-"Hi-Fi") VCR and a plug-in processor probably would not be taxed, whereas an integrated product would certainly be taxed. All you would be doing with this bill would be to deny society the considerable design, production and cost efficiencies of product integration.

S. 1739 Is Fatally Flawed, Even As It Applies to Existing Audio Products.

It isn't necessary to project into the future at all to discover fatal technical flaws in S. 1739. The bill purports to call for regulations to extablish "exemptions" for tapes that are not suitable for high quality musical programming. My own experience with tape testing convinces me that in the practical world of magnetic tape technology, this is simply an unrealistic proposal.

Tape Cannot Be Classified According to Use

To begin with, any one of the four current generic types of tape may be used for any recording purpose. The generic categories of tapes now designated as Roman numerals I, II, III and IV are simply assigned as an aid in identifying required recording parameters on a tape recorder, so that it will work properly with that particular generic type of tape. Within each generic category, the tape manufacturer may have any number of tape Grades. Each Grade is capable of making "high quality" recordings of audio programs. Thus, a type I tape may easily make a better audio recording than a type II tape. Indeed, the "quality" of the tape can never be judged in isolation-- it all depends on the design parameters of the recorder(s) with which the tape will be used. In my view, attempting to classify tapes in terms of their intended use is not only impractical; it is for all intents and purposes impossible.[4]

What I have said about the prospects for classifying tape according to intended use is true even as matters stand now. But again looking to the near future, and at the technology that already exists in the laboratories of hardware and software makers, such categorization of tapes may be entirely meaningless in a year or two. The industry has already developed standards for dedicated home digital audio tape recorders. In the case of digital tape recording, the quality of the tape formulation has little to do with the quality of the recording that is made. In fact, one of the chief virtues of digital tape recording is that even tapes that would add very high levels of noise or tape hiss when used to make conventional "analog" audio recordings are perfectly suitable for use in a digital audio recording system.[5] That being the case, I fail to see how any grading of tape types would serve to identify the uses to which those tapes ultimately will be put.

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[4] I endorse without qualification the excellent and complete testimony given on this subject by my friend and colleague Mr. Ed Foster before this Subcommittee on October 25, 1983.

Recorders Cannot Be Classified According to Use

It is, and will continue to be, similarly artificial and destructive to attempt to classify recorders according to whether they will be used to store prerecorded music or to record or play something else. You don't need a technical background to be aware of the most basic argument against such an attempt -- the fact that music is music. Thus, a recorder on which I might tape or play a recording of a Chopin piano sonata is one I would want to use also to record my practice on my own piano. Indeed, from a technical viewpoint, I should really state the proposition the other way round: The recorder on which I will wish to record my own piano practice will without doubt be one that I also consider suitable for recording and playing prerecorded music.

But even if you are prepared to be grossly unfair to the millions of amateur musicians in this country, you are still not much closer to having a fair and workable tax on recorders. My knowledge of technical trends leads me to conclude that it will be impossible to maintain any viable distinction between recorders used primarily for music and recorders used primarily for the spoken word. As to today's products, I call your attention to the common portable stereo cassette recorder / player, or "boom box." In the playback mode, these recorders are used both for music and for voice, although my trips to the beach tell me that playing back music predominates. These units almost all have built in microphones, however, as well as switches and jacks that permit users to make recordings from internal and external sources. The quality of such recordings often rivals those made on "home" recorders. (Whether this is "high fidelity" depends on the price of each unit, the type of tape used, and your personal standards.) Yet, recordings through the built-in microphone, and many through external microphones, are likely to be, very often, of the spoken word.

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[5] This is so because a digital recorder reads the presence or absence of electronic pulses used to encode a signal. Even when an inherently "noisy" tape is used, the detection of the presence or absence of pulses is undisturbed, so performance is unaffected. This should enable the recording industry to market digitally recorded prerecorded tapes on relatively inexpensive tape, without sacrificing quality.

In recent years, the "boom box" has been joined by its smaller and even more portable cousin, the Walkman-type player and recorder. Already, some of these handheld units are capable of performance in the recording mode that rivals "home" decks of similar price. I have such a unit. I have personally used it for "in the field" recordings of musical performances, with entirely satisfactory results. I also use it to record speeches, conferences, and panel discussions. In this context, its stereo capability is extremely helpful, as it permits me to better identify who is being recorded. In my opinion, handheld devices on which I would be pleased to record live or prerecorded music will soon be available to average consumers, and they will also be the most popular devices for recording the spoken word. The development of such popular all purpose recorders will be denied to us only if one of those purposes is taxed.

The Inevitable Inequities and Distortions

Let me just mention two more examples, from the trends I have discussed, to demonstrate why this bill is unfixable. How are you going to treat the hand-held, multi-purpose recorder that I have just described? As presently written, S. 1739 would tax it. Should the Copyright Royalty Tribunal create an exemption for this product? If it does not, the Tribunal will penalize all those who want to own the best and most flexible hand-held recorders, including journalists, businessmen, educators, etc. It will create disincentives to the production of such recorders. If it does create an exemption, and limits the tax to non-portable decks, pretty soon most high quality decks will meet the definition of "portable" -- it will be cheaper for the manufacturer to add the portability feature than to pay the tax. If the rationale for this legislation is to be maintained thereafter, the Tribunal would have to abolish the portability exemption and go back to taxing all recorders. This is why I firmly believe that an exemption that would actually work "as advertised" is simply not possible.

Returning to the "video" world, let us calculate the "audio" tax imposed by S. 1739 on existing video recorders and tape. On a Beta or VHS "Hi-Fi" recorder that sells for $500 , the recorder tax would be $25. As to tape, a standard T-120 tape -- the one most commonly sold by video retailers and others who sell video tape -- would incur a tax, at the wholesale level, of $3.60. At retail, this would effectively double its purchase price. As to tapes used with several 8mm "video" recorders that are already on the market, the tax would be $7.20.

What could the Tribunal do about this result? The tax rate is fixed by S. 1739. The choice would be to exempt a particular product or not to exempt it. This decision is arbitrary with respect to presently available products, and any outcome would distort future developments. And with respect to the products that will be available in the near future, there will be no basis at all for the Tribunal to decide: to tax or not to tax.

One might respond, of course, that the answer is to be sure to tax all new recorders and media -- audio, video, computer-- irrespective of the consequences. Mr. Chairman, based on thirty years experience in this industry, I can tell you that this would not only be unnecessary; it would also be the greatest assault on technological innovation, and the benefits it offers society, since the Luddites. It would be unnecessary because every innovation I have witnessed, from color television through the video recorder to the compact disc, has proven ultimately to be strongly to be benefit of suppliers of programming. One might have thought that adding color to television would weaken the theatrical market for movies. And some people did think that the VCR would do this. Instead, the hugeness of the new markets that have been opened has become obvious to virtually everyone.

I refer to the Luddites because history has shown that you cannot suppress technological progress and you regulate it only when you must. The video recorder, the Walkman and the compact disc player -- indeed, the microphone, the amplifier, and the phonorecord -- were not free goods, willed to the entertainment industry. Nor were they invented by the entertainment industry. Opening new markets is expensive; shaping them is risky. It is a process that, in our society, we have left to free enterprise, rather than the hand of government. It is to this freedom of others to invest in new technology that I attribute much of the success of the recording industry, as well as other software proprietors. I see nothing on the horizon that I have surveyed for you today that threatens to diminish this success in any way -- if the government will only stay out of the picture.

Mr. Chairman, having reviewed the provisions of S. 1739, considered how it would operate on the products with which I have worked, and thought about ways in which the bill might be revised, here is my conclusion. This legislation is fundamentally at odds with the realities that govern home recording today, and will shape technology tomorrow. The very idea of having the government officially distinguish "audio" recording devices and media from "video" devices and media is not just obsolescent; it is obsolete. The idea of a royalty tax on multi-purpose recorders and media is distortive, even destructive, of socially beneficial technology. Even from the most narrow, short term perspective, attempting to apply this bill to the products available today will punish huge categories of users and harm the public, as potential developments of general application are forestalled by this tax. I urge you and the members of the Subcommittee not to adopt this, or any, tax.

Thank you for inviting me to appear today.

Senator MATHIAS. Ms. Foreman.

STATEMENT OF CAROL TUCKER FOREMAN

Ms. FOREMAN. Mr. Chairman, I am Carol Tucker Foreman, president of Foreman & Co., and formerly executive director of Consumer Federation of America. I am here today representing the Audio Recording Rights Coalition and the millions of Americans who own and use audio recorders and tapes in their homes and offices. The Audio Recording Rights Coalition includes State and local consumer organizations and tens of thousands of individual consumers from all across the country, who have joined with us in opposing the goals of S. 1739. In addition to ARRC, the Consumer Recording Rights Committee has representatives from many consumer groups, including the Conference of Consumer Organizations, the Arizona Consumer Council, the Pennsylvania Citizens Consumer Council, the Rhode Island Consumer Council, the Pennsylvania League for Consumer Protection, the West Virginia Consumer Federation, Maryland Citizens Consumer Council, Consumers Association of Kentucky, West Virginia Consumer League, Cleveland Consumer Action, and the Maryland Public Interest Research Group.

If S. 1739 becomes law, consumers would pay a tape tax every time they buy audio and video blank tapes or recorders. They would pay no matter how they use the tapes. We do not believe that logic, equity, or the Constitution support using Government power to shift large amounts of money from individual consumers to recording industry giants. There is no consitutional requirement for S. 1739. The recording industry is healthy and does not need a new infusion of funds from consumers, and there is no reason to believe funds collected would accrue to struggling artists. The proposed remedy is inequitable and quite probably unworkable. What I would like to explore with you today is the why of the whole idea.

Before acting on this legislation, you must ask yourselves, why should consumers pay? The recording industry has told you we should pay simply because there is a copyright issue involved. They argue that the existence of a copyright constitutes an automatic entitlement to more revenue. There is no basis for that argument. Copyright does not have some a priori meaning, and there is no natural law or philosophical or logical underpinning that guarantees the copyright holder more money whenever he or she asks for it. A copyright is a legislative creation, not an automatic money-making machine.

Article I, section 8, of the Constitution and the interpretation of it over the years makes it clear that the copyright process is a balancing act. The Constitution admonishes Congress to satisfy the artist's desire for reward only as a means of satisfying the public's need to have access to the copyrighted material. Congress is not obligated to say yes to copyright holders. You should award them more money only when it is essential to keep creators creating. When the creative flow is already heavy and the rewards are already high, Congress should not act.

Congress is essentially cast by the Constitution as the assessor of how much is enough, of how to balance consumers' interests against copyright holders' interests. In doing this, Congress has consistently recognized that copyright owners' desire for more money is not by itself a proper justification for extending copyright.

But Congress' consistency has not been matched by others, and some people keep forgetting this framework: that copyright refers to the delicate balance between a creator's desire for higher rewards and the public's need for easy and inexpensive access to their creations. Before Congress decides that a shift of money from consumers to the recording industry is warranted, Congress needs to return to the framework underlying copyright and ask some fundamental questions like: How much is enough? How much money do artists need to induce artistic output? These are not easy questions to answer, but their difficulty does not justify assuming that there is no limit to what copyright owners should receive.

Creative and artistic output is very high—so high that it seems like there should be enough money in the system to elicit all kinds of new music. For example, many new women country artists have emerged lately—artists like Janie Fricke, Reba McEntire, Pam Tillis, Rosanne Cash, and The Judds. In rock, Wham, Squeeze, Tears for Fears, and the Thompson Twins are all hot. It may not sound like music to this subcommittee, but it is to the millions of kids buying their records. Would more money to the copyright community make any difference? Is Wham going to quit next week? Is Madonna going to give up recording for housewifery because the rewards are not sufficient?

It is also hard to justify handing over more money to the record industry when you take a look at its profits in recent years. The record industry enjoyed a record high $4.5 billion in sales in 1984.

Does it sound to you like this is an industry unbalanced by low profit?

I want to take a minute here to remind you that the recording industry's profit and loss is the right focus. It is not wrong or crass to talk about money when it comes to copyright—because that is what copyright is about, money, and who gets it, and who loses it.

Every time you hold a hearing on this subject we hear a lot about the poor starving artists, the young person who needs to be encouraged to create. However, the proponents of S. 1739 are a little less benevolent in their concern than it would appear. The legislation provides that royalties will be distributed to the "owners of copyrights in musical works and sound recordings."

Who are these folks? One of them is Michael Jackson, a poor young man from California. Not too long ago he paid $47 million for the music publishing rights to almost everything Paul McCartney and John Lennon wrote between 1964 and 1970. He will now get copyright royalties whenever one of the McCartney-Lennon records is purchased, played on the radio or television, or used in movies.

This bill would provide royalties to Michael Jackson. But it will not be to Michael Jackson, the artist, the creator; it will be to Michael Jackson, the music publishing tycoon. This very rich young man has discovered that he can get richer—not by writing more songs—but by buying the rights to someone else's creativity. I do not think he needs or deserves any money that S. 1739 would hand over to him because he was rich enough to buy Lennon's or McCartney's work.

I have talked to copyright lawyers, and we have searched and searched in the words and between the lines of this bill. We just cannot find where the bill says the tape tax proceeds will go to Joe Struggling Artist. Take another look at the bill and see if you see Joe Struggling Artist in there. All that is in there is Michael Jackson and CBS and Warner. They are not starving artists, and giving money to them does not equal increased creativity.

The fact that the record industry is doing well, both in terms of new artists and great profits, gets back to another basic issue, too, and that is the allocation of the burden of proof. Does the recording industry have to prove entitlement to more money or should consumers have to prove their right not to pay more? With a system that is already nicely in balance between the copyright holders and consumers, Congress should require the copyright holders who want to change the status quo to bear the burden. Congress should put them to the test, and make them really shoulder the burden of showing genuine harm from taping. And in scrutinizing claims of harm, Congress should remember the boy who cried wolf.

At a time when the recording industry is doing so well, it does not seem fair to make the consumer pay a tax to create his own tape of his favorite songs from different albums in his collection, or pay to rearrange the contents of a particular record to suit her tastes. The music lover who tapes a record she bought to use in the cassette player in her car should be free to do so. She should not have to buy the record and the cassette of the same album So often, she can make a higher quality tape at home than she could buy at the store. Again, those questions of why should the consumer pay and how much is enough are exactly the right ones to ask.

And let us not forget the real injustices S. 1739 does, in the name of copyright, to people whose taping never gets close to a copyright. The record industry is trying to make consumers pay when they use cassettes to tape a child's first piano recital or a religious sermon on the radio.

Whatever exemption the bill provides for noninfringing uses will still be an added cost to the consumer. How will the exemption work? Will the elderly woman taping sermons off the radio have to pay the tax and then prove she is not using it for the wrong reasons? In fact, all this bill does is unfairly shift the burden to consumers to prove they are using the tapes they buy for noninfringing purposes. It is changing that delicate balance, and it does not seem fair.

Consumer Federation of America has been sensitive to the balancing arguments in this debate. The Nation's largest consumer organization understands that the public has an interest in encouraging artists to create. However, after examining this issue, the Federation's annual meeting came down on the side of the balancing function inherent in the constitutional provision. They approved the following resolution:

> CFA urges Congress equitably to resolve the rights of consumers and producers of home entertainment. This resolution should clarify that consumers who engage in home copying of video and audio programming for personal use do not violate the rights of copyright holders. Congress should also examine whether home copying by some consumers, in the aggregate, causes economic loss to copyright holders that in the long run is likely to reduce the variety of home entertainment available to consumers. If Congress finds such injury, it should enact legislation that will provide just compensation to injured copyright holders to the extent of their injury in a manner that imposes royalties equitably on those whose copying is the cause of the injury. The method of redress should provide for effective consumer participation or representation on the assessment and distribution of royalties.

Consumers Union of the United States has taken a similar position. In fact, Mr. Chairman, I cannot find any consumer who is anxious to have the Government impose a tape tax. In the final analysis, this bill is about using Government's power to shift money from one set of hands to another. It is about the Congress voting to take money from consumers and hand it over to recording companies. The recording companies have not made the case. The balance is on the side of consumers. The proposed shift is unfair and unwarranted.

Senator MATHIAS. Thank you.

[Following responses were subsequently submitted for the record:]

Responses of Carol Tucker Foreman to Questions Submitted by Senator Mathias

Ms. Foreman:

At the October 30, 1985 hearing, Mr. Gortikov showed the subcommittee charts indicating that the blank tape manufacturers market their wares based on qualitative differences and specifically recommend different tapes for different kinds of music. Experts who testified with you stated that all these tapes are suitable for all kinds of music, and that the difference in quality among machines can overwhelm the distinctions in tape quality.

a- As a consumer advocate, how do you feel about these seemingly conflicting assertions?

b- Do you believe that consumers are satisfactorily informed by tape manufacturers that all audio recording tape is actually capable of recording music?

c- What is your opinion of the wide variation in marketing, labeling and pricing given the relative substitutability of audio recording tape?

Let me begin to respond to the part of your question concerning seemingly conflicting assertions by Mr. Gortikov of the RIAA and experts who testified as part of the ARRC panel. Mr. Leonard Feldman said during our appearance before your subcommittee:

> Within each generic category, the tape manufacturer may have any number of tape Grades. Each Grade is capable of making "high quality" recordings of audio programs . . . . Indeed, the "quality" of the tape can never be judged in isolation -- it all depends on the design parameters of the recorder(s) with which the tape will be used. In my view, attempting to classify tapes in terms of their intended use is not only impractical; it is for all intents and purposes impossible. [Footnote: I endorse without qualification the excellent and complete testimony given on this subject by my friend and colleague Mr. Ed Foster before this Subcommittee on October 25, 1983.]

In his statement submitted for the hearing record, Edward Foster reiterated the points made in his 1983 testimony:

> I also stated that the quality of a recording is not determined solely by the tape that is being used, nor solely by the recorder, but by the relationship between the two and that "high fidelity" is what is perceived as high fidelity in the mind of the listener. The same is true today.
>
> * * *
>
> Indeed, not every user wants the same tone quality. What is "high fidelity" to one listener is not to another.

Clearly what Messrs. Feldman and Foster said is that there are objective differences in specifications and price of both tapes and recorders. There are also differences in consumers' ability to hear or concern about those differences. Some of us can hear the difference in quality between a cheap tape and a good one no matter what kind of machine it is played on and some of us can't or may not care. It doesn't seem inappropriate to me for manufacturers to emphasize the superior qualities of their top of the line, high performance product. That does not mean, however, that lots of consumers won't be satisfied with something less than top of the line.

You asked if I believe that consumers are satisfactorily informed by tape manufacturers that all audio recording tape is actually capableof recording music. In preparing to answer your question, I went over to Tower Records and picked up some material available at the tape display. I enclose a page from a brochure that was displayed. There is more information here than I need or understand. The differences are important to some consumers. They want this kind of detail and it is clearly available to them. I think everyone understands that the least expensive tape is capable of reproducing music. Most of us understand that some of these tapes will do that better than others and we choose based on a balancing between desire for quality and price.

Finally, you asked my opinion of the wide variation in marketing, pricing and labeling of tape given their relative substitutability Once again, Mr. Chairman, all recording tape can be used to tape music. Some will be satisfied with the performance of a cheap tape. Some will insist on only the highest quality reproduction.

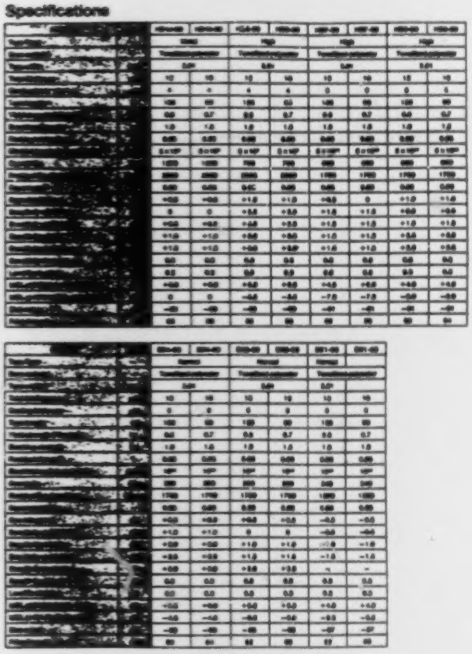
Other factors such as tape and shell durability, labeling material, and physical appearance of the shell may influence the buyer. I don't know how much these factors add to the cost of a tape. Information is widely available, however. We may all get a little weary of advertising hype but most consumer groups have followed the general rule that, unless a product is inherently very dangerous and cannot be used safely, we should just make sure that information is complete and easily available and let the market do the rest.

Finally, Mr. Chairman, it seems to me that the disagreement here has arisen because the recording industry wants a copyright fee attached to tapes and recorders. They are having a real hard time coming up with a scheme that doesn't penalize those who never tape copyrighted material. They are grabbing at straws. One of the straws is this classification system. It just won't support their case.

DENON

CASSETTE TAPE

Specifications



Measurement conditions:
- Unit: 0 dB = 250 pWb/mm
- The values are the difference between the following tapes
  HD-M: CMP-460-1061
  HD6, HD7, HD8: CMP-260-1061
  DX1, DX3, DX4: CMP-[illegible]-1061

* Specifications are subject to change without notice

Ms. Foreman:

Toward the end of your written statement, you cited the resolution of the Consumer Federation of America. That resolution seems to call for just compensation for the copyright holders if Congress finds that they are being injured by the practice of home taping. If Congress does so find, what mechanism would you recommend, in keeping with the resolution of the CFA? I realize you oppose the approach in S. 1739, but what alternative would you support if Congress makes the threshold judgment that consumers are being indirectly harmed in the long run by the direct injury suffered by artists in lost sales due to home taping?

The CFA resolution calls for Congress to examine whether "home copying by some consumers, in the aggregate, causes economic loss to copyright holders that in the long run is likely to reduce the variety of home entertainment available to consumers." I do not believe there is any evidence of such injury. I would also note that Mark Silbergeld of Consumers Union, in his November 1, 1985 letter to Chairman Mathias (attached), agreed that the recording industry has "failed even to show that home recording of copyright audio works results in any net loss to copyright holders, much less a loss sufficient to threaten creativity."

The music industry is quite healthy. Not only are revenues and profits up for the industry as a whole, but new releases of music are on the increase. And this increase is occurring in spite of internal business decisions to focus on fewer acts.

Be that as it may, even if there were a showing of decreased availability of music and it could be shown home taping was responsible (a relationship which has yet to be demonstrated), the CFA resolution contemplates imposing "royalties equitably on those whose copying is the cause of the injury."

No legislation yet proposed has come close to satisfying that directive. I am personally at a loss to figure out how to craft legislation which does not end up inequitably assessing royalties against those whose use of blank tape and recording equipment has nothing to do with copying prerecorded works. Furthermore, as I stated in my testimony, the burden of drafting such limited legislation is on those who seek to extend and increase copyright protection. Both because I see no need for such legislation and because I doubt I would have any better luck than the Recording Industry of America which has for years tried and failed to draft such legislation, I can offer no better idea how it could be done.

Consumers Union

Publisher of Consumer Reports

November 1, 1985

Honorable Charles McC. Mathias
Chairman, Subcommittee on Patents,
Copyrights and Trademarks
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I would appreciate inclusion in the hearing record of this statement of Consumers Union's firm opposition to S.1739, which would impose on all consumers of blank audio recording tape and home recording equipment a tax meant to compensate the recording industry for insufficiently substantiated claims of lost sales due to home copying of copyrighted works by some limited number of tape and equipment purchasers.

The Copyright Act does not and should not guarantee to the holder of any copyright payment for each and every copy of the copyrighted work that another may enjoy. It intends, rather, to provide such protection as encourages ongoing creativity from which society as a whole will benefit. The copyright holder's profit derives from that basic societal interest.

Therefore, any claimant to a legislative right to increased profits from the sale of copyrighted works, where there is no loss from legally defined infringement, bears the burden of showing not only that the asserted injury is real, but also that it results in reduced creativity. We do not believe that this week's hearings before the Subcommittee have substantiated such a claim.

And, indeed, the legislation now before the Subcommittee would require the revenues from the proposed tax to go not necessarily to the creator of the work but, rather, to the copyright holder. The copyright holder may well be a very wealthy artist or a large record company, not a struggling composer or performer.

The recording industry as a whole enjoyed record high profits in 1984. The dip in profits preceding 1984 occured during a very serious recession, when virtually every industry suffered. And it occured during the height of popularity of the popularity of video games, a strongly competing form of home entertainment. The recording industry seems to have fully recovered. And the advent of the compact disc promises a future windfall to the recording industry, as music lovers replace existing recordings already in their library with new performances of the same works, and even with the same performances in the new format, in order to enjoy the new technology. There is absolutely no evidence of decreased incentives to create new audio home entertainment programs.

Indeed, we believe that witnesses who have urged passage of S.1739 have failed even to show that home recording of copyright audio works results in any net loss to copyright holders, much less a loss sufficient to threaten creativity. It is remarkable that witnesses at this week's hearings refused to provide the Subcommittee with individual firm profitability data needed to confirm their own claims of injury.

Studies of home copying behavior performed for the recording industry and the electronics industry claim, not surprisingly, startlingly differing results. The recording industry studies claim to demonstrate that a high percentage of all copying activity simply reproduces a copyrighted program "as is" to bypass a purchase. The electronics industry studies claim to demonstrate that the net effect of home recording may actually increase the sale of copyrighted materials. The latter studies report that many copyrighted recordings are purchased because the buyers wish to use them to arrange their own tape programs from multiple recording sources. They also suggest that "as is" pass-ons from a purchaser of a commercial recording to a non-purchaser may result in the non-purchaser's subsequent purchase of other copyrighted material by the same recording artists.

We are not prepared to judge the relative competence and merit of these individual surveys. It should suffice that the recording industry, which should have the burden of establishing its conclusions of fact over competing, contrary conclusions, has to date failed to do so.

We must add, however, that certain qualities of copyrighted commercial recordings create legitimate consumer incentives for copying such materials.

First, production of many items tends to terminate long before the copyright expires, creating a legitimate consumer incentive to copy instead of purchase simply because the item is no longer available for purchase. Second, when there are no pressing defects, a vinyl disc is typically superior to the commercial cassette version of the same program, creating a legitimate consumer incentive to purchase the vinyl disc and create a home cassette copy for portable listening. Third, vinyl discs are subject to serious damage and wear, creating a legitimate consumer incentive to copy purchased items in order to safeguard the investment in the disc.

Thus, while no one can seriously deny that some home copying displaces sales, the appropriate questions are, "to what extent" and "are these offset by sales generated by home taping"? The three factors we have identified and those reflected in the studies performed for the electronics industry indicate that there are legitimate motives for home taping which do not displace sales, and which may offset or generate additional sales that exceed losses from copying which does displace sales.

Even were new evidence to show a loss of sales sufficient to reduce creative incentives throughout the recording industry, the method of compensation proposed by S.1739 is unfair and onerous to those home recordists who do not engage in copying that displaces sales. Every consumer of blank tape would pay a roughly estimated one-third more at wholesale for every tape they purchase, an additional ten percent more at wholesale for every home recorder they purchase and an additional twenty five percent more at wholesale for every dual home recorder they purchase. With retail markups, prices can be expected to exceed even these substantial increases. And they would apply regardless of whether or not the use of the equipment and tape replaces the sale of a copyrighted work.

In short, S.1739, despite its lack of firm evidentiary support, would substantially increase the price to consumers of this popular form of home entertainment.

For these reasons, we strongly urge you not to report S.1749 to the full Committee.

Respectfully,

/S/

Mark Silbergeld,
Director, Washington
Office

CC: Senator Laxalt
Senator Hatch
Senator Simpson
Senator Leahy
Senator Metzenbaum
Senator DeConcini

Senator MATHIAS. Mr. Graves.

STATEMENT OF J. SCOTT GRAVES

Mr. GRAVES. My name is Scott Graves, manager, VESCO, in Rutland. I am submitting this statement in opposition to S. 1739, the Home Audio Recording Act.

My purpose in submitting this statement is to urge this committee to expand its focus in examining the home taping issue. For years, this committee and much of the Congress as a whole have heard the repeated complaints of the U.S. recording industry. The industry has told you that each year it loses $1.5 billion to the evil of consumer home taping, and for some reason a lot of you believe that grossly inflated figure. As a result, legislation has been introduced to tax blank audio tapes and audio taping equipment. What is more, punitively high taxes would be placed on dual-head cassettes, which the consumer is more and more clamoring for.

Members of the committee, the giant companies that make up the recording industry are not the only parties with economic interests in the outcome of this latest episode of home taping legislation, and the truth is not solely the subjective truth as they see it and feed it to you. Retailers and consumers also have interests, and truth in this area cannot be arrived at unless you hear their sides as well.

I have been in the music retailing business for 2 years and today manage the Woodstock outlet of the seven VESCO stores. The sale of blank tapes and audio equipment represents approximately 25 percent of my business, the remainder comprising sales of appliances and lighting, as well as records and prerecorded tapes. Every day I and all my store personnel deal with consumers coming through the door to purchase the merchandise and equipment that would be subject to your new tax.

My customers are not pirates. Many of them buy tapes and equipment for other uses, as well as for taping prerecorded music. And even when they are using these items to tape prerecorded music, they do not see themselves as stealing money from the recording industry. Indeed, as a general matter, most of the tapers in my stores are the same ones who go over to the album racks and the compact disc racks and the prerecorded cassette racks and represent the highest volume purchasers of all those items. Often, of course, the two purchasing activities go hand in hand, since the blank tape is used to record the record so it can be played in the car or in the walkman device. This is not an act of thievery, and neither my customers nor I can see any reason why they should be penalized as if it were.

But I am not offended for my customers' sake only. I read the papers, and supposedly this is a time when taxes are going to stop their ever-upward spiral and small businessmen like me are supposed to enjoy incentives to thrive and expand and create jobs for ourselves and our communities. When I look at this Home Audio Recording Act, however, all I see is a Congress poised to tax me so that the huge companies behind this legislation can take money from me and my customers and stuff it into their already overflowing coffers. Big business should have its breaks, too, but those breaks should not be excessive and undeserved, and the breaks should not break the backs of the small businesses and consumers who would be forced to cough up millions of dollars under this bill.

In closing, I want to comment briefly upon the creative artists who the giant record companies would have Congress believe they are representing. First of all, everyone knows that the artists who stand to see any of my dollars are the successful ones who could buy my entire business and not even notice that any of their dollars are gone. The other artists, the struggling ones, are not likely to see any of my money. In fact, they are likely to add to it, since the struggling artist is just a consumer by another name. He comes into my store and he buys taping equipment and blank tapes to tape his practice sessions, and he is the one who cleans out my record, disc, and prerecorded tape displays. Before this struggling artist would ever see a single dollar from this legislation, he would pay a whole lot more of them in order to further enrich the already successful superstars and to prop up the record companies who could, but will not, give him a contract.

Senators, I appreciate having been given the opportunity to express my views, and I believe, the views of retailers around the Nation, on S. 1739. I hope that my remarks will be useful to the members of the subcommittee as you consider this bill, and I trust that ultimately you will reject this unfair and unnecessary proposal.

Senator MATHIAS. Thank you very much.

Unfortunately, we have another rollcall vote in progress. Let me get a question in before I have to go.

Mr. Battaglia, you said you were outraged by the possibility that your business might be taxed, and I can understand that. Nobody likes to pay money they do not have to, but put yourself in the position of this committee and look at the problem. Put yourself in the position of having gone to a conservatory of music, working your way through, serving hamburgers at McDonald's, to get yourself through the conservatory, and going on to become a professional song writer or a professional singer, or some other creative talent involved in the entertainment industry. Then, after those years of preparation, you had reached the point where you were earning pretty good money and you could make records expecting to be able to earn a profit from them, and you find that instead of your cashing in, other people are literally stealing your talent, taking it for nothing. How do you think you would feel? Mr. Weiss and those in the Songwriter's Guild are outraged.

I can understand your sense of outrage. Can you understand their sense of outrage?

Mr. BATTAGLIA. Senator, their outrage is based on the business decisions. There are financial rewards for their chosen career. I do not understand their outrage.

Senator MATHIAS. What kind of a business decision is it? Let us use an analogy. I do some writing every now and then, so it is not too farfetched. I write a book, and one of the reasons I write it is to make a profit. Dr. Samuel Johnson said only a fool would write except for money.

So I anticipate a profit when I write that book. Otherwise, I might have gone out and had fun in the evening instead of scribbling away.

Let us say my publisher does not have very optimistic prospects about the book so he only issues a limited number of copies. If somebody buys one copy and pays me the royalty on one copy, and then runs it through a sophisticated copying machine and makes a couple of hundred copies, is he not stealing royalties from me for those copies that he duplicated without my authorization?

Mr. **Battaglia**. Senator, the people who use blank tape do not steal from recording artists. They make the attempt to tape the merchandise they purchased. They bought that. They want quality sound. Record companies will not give them quality sounds on tape. The consumer is forced to get quality sound by using a blank tape, making his own version of that compact disc for use in his car or in his Walkman. He is not stealing.

If the record company wants him to buy the tape, they better start making quality products.

Senator **Mathias**. Do you ignore the fact that there is something called intellectual property?

Mr. **Battaglia**. I believe there is intellectual property.

Senator **Mathias**. When you buy a book, you are not just buying a pad of paper. You are buying the thoughts recorded on that paper. Is that not true?

Mr. **Battaglia**. Yes.

Senator **Mathias**. When you buy a tape, you are buying the music, the sound, the ideas expressed in the music or voices that are recorded on that tape. Is that not true?

Mr. **Battaglia**. Yes.

Senator **Mathias**. Well, that is what we are trying to protect, and that is why these artists are outraged, because people are stealing that.

Mr. **Battaglia**. Senator, the royalties that are paid to the artists when they buy the compact disc or record, if the consumer says that there is an additional market here for quality music, for your music, it is the problem, in your analogy, the publisher that is not serving the artist properly, the record company refuses to take the artist's material and puts them on acceptable quality blank tapes. That is why consumers will not buy them. Your publisher is your enemy, not the blank tape company.

Senator **Mathias**. Can we not agree that the unauthorized acquisition is an invasion of the artist's rights?

Mr. **Battaglia**. Senator, I do not know the answer to that. I feel I have the right to tape my own records. I do not really know. I am not a lawyer.

Senator **Mathias**. Your business is about a $3 billion business, is it not?

Mr. **Battaglia**. Yes. Blank tape is a small part of it.

Senator **Mathias**. How much would this affect the profitability of the division?

Mr. **Battaglia**. This would affect the profitability of the division of which I am responsible. Our margins are very low on blank tape, and unlike others, I would welcome you to look at our books for the division.

Senator **Mathias**. Ms. Foreman, I want to say that I agreed with you when you said the copyright laws do not guarantee income. Copyright laws should not guarantee money. If you copyright a poor product, you are going to get no more out of it because it is copyrighted than because it is not copyrighted.

What copyright laws intend to do is to provide some protection for the creator of intellectual property, whether it is the written word or musical composition, a work of art or a painting. We do not desire to guarantee that a creator is going to make a profit, but simply that if he creates a valuable product, whatever property rights he has in it are protected. This is not unlike the way in which we protect the farmer who owns the field and is entitled to reap the crop that grows on that field. What is wrong with that?

Ms. **Foreman**. Sir, you and I have rarely disagreed over the years that you have been here and I have been here, and I am sorry we disagree on this one.

Senator **Leahy**. This is a question that I will ask of each of you when we come back. I get the impression that Mr. Battaglia thinks of this as economic guerrilla warfare and not as a problem involving our recording artists. I think you might want to think carefully of your answers. The question I am going to ask is this: if I hear a record I like at a friend's home, and I borrow it and make a copy or a tape of it for myself, should I pay for the use of that music? I will ask that question of each of you when I come back.

[Short recess.]

Senator **Metzenbaum**. The hearing will reconvene. Come to order, please.

I will just throw my questions out, and whoever wishes to can pick them up.

Mr. Greenspan has testified that the number of total releases has gone down significantly over the last few years. Is that true? And if it is true, how do you explain it?

Mr. **Ferris**. I think the record companies have changed their own personal judgments of how they are going to use their resources. They are not funding apparently as many artists as they did before, but they are making record profits, so apparently they have changed their method of how they are doing business, and it has turned out to be an extraordinarily profitable decision.

I do not think there has been anything official in the record this morning, Senator, that purports to say that there is any particular type of artist that is deprived. None of the witnesses of the recording industry have provided that, and I think there is still the widest range of music being provided.

Senator **Metzenbaum**. They say their profits have gone down. You said they have gone up. We have some evidence with respect to some companies. We do not have it with respect to all of them.

Do you have any further confirming evidence that their profits have gone up other than the ones we have mentioned?

Mr. **Ferris**. The only evidence I have is from the trade press, Senator; that 1984 was the highest profit year for the recording industry.

Senator **Metzenbaum**. That the trade press reports that statement as such? Do you have that with you?

Mr. **Ferris**. Yes. I will put it in the record.

Senator **Metzenbaum**. Would you read what the heading is on it, please.

Mr. **Feldman**. Senator, I think in answer to your question, there is another technical aspect to the answer, and that is, as you well know, we have now come upon a new technology known as the compact disc, and part of the reason, I think, for the fewer releases is the lack of supply to come up to meet the demand of the compact disc. There is even an item in the paper today that confirms this fact. The demand is tremendous for the laser read compact disc, and the record companies have lagged again just as they did in the case of quality cassettes, by not meeting that demand punctually and properly, and, therefore, they have had a slackening in the purchase of conventional LP records by those people who would rather buy the new medium, the compact disc.

Senator **Metzenbaum**. You are saying their failure to record more is by reason of their not being prepared for the laser discs?

Mr. **Feldman**. That is correct, sir, and that is the fault of the record industry.

Ms. **Foreman**. Yes, sir. I have got a transcript from the Strictly Business television show from August 10, 1985, in which John Cafferty, who is Columbia Records' vice president, I believe, says that the advent of the music video, and especially the 4-year-old cable phenomenon, MTV, which plays the music, has also increased the cost of introducing new artists. He says this is one of the reasons why they have stopped putting out so many new——

Senator **Metzenbaum**. I do not understand that. Why has MTV, and whatever else, is an increase in cost. I do not understand the rationale.

Ms. **Foreman**. Because the promotion costs of the record are so much more expensive, they must reduce the number of units they sell. Mr. Cafferty says they feared sales would fall dramatically, but it did not turn out that way. Mr. Swindler, the manager of Power Records, stated:

> It saved us an enormous amount of money on our shelf space and return, and this appears to be a shaking down within the industry, where they find that it is very expensive to promote large numbers of new releases. Therefore, the number of new releases that they have put out has been judged by a much more stringent standard than it was before. It should not be interpreted that they have lost substantial amounts of money because the record here indicates that it did not.

Mr. **Ferris**. I have the citations but not the articles. I can give you three or four citations. Billboard, March 23, 1985. It is 1 year for records, Fortune, April 1, 1985, RCA Reports. I am just giving the citations of the trade press. I do not have copies of the articles, but I will provide them for the record, Senator. All support the fact that 1984 is the highest year for profits in the record year.

Senator **Metzenbaum**. Why do you not get a copy of that for my staff.

Is it your position that the industry does not indeed deserve any compensation, even though they are losing some sales? I have some difficulty with this whole subject because it seems to me that there are some equities on both sides, and some illogical on both sides, and I am not sure that I can make logic of some of these illogical questions that hang over this issue.

Tell me, how do you justify the right of somebody to make the copy of somebody else's product? It would seem to me that if you had a bill that provided that every time you made a copy of a cassette that cassette required you to put a nickel in the slot, or dollar, whatever the price might be, that that would have some merit to it. It seems there is some right for the composer and the performers, as well as the record producers, to have some compensation.

Do I understand your position to be that they are not entitled to anything?

Mr. **Ferris**. Our position is, Senator, that they are entitled to royalties on their creativity, and they get it. When I go down to the store to buy a record and bring it home, they get a royalty which they negotiated, depending upon their bargaining power, with the record industry on that record sale. What all the new technology has provided, Senator, with new cassettes, has provided me with that opportunity to take that record home and copy it on my cassette player, so I can hear it not only in my home, but in my automobile, that I could hear it on my Walkman as well.

The notion that I would buy another record——

Senator **Metzenbaum**. How do you distinguish that from the fact that you buy a book, and with the new procedures available, you can make copies of that book and have one copy at the office and one copy at another place in the house? I guess technically you are violating the law when you do that, because it is copyrighted material. You do not have the right to do that. You may not be prosecuted, but that does not mean your actions are legal.

Now, how do you distinguish that in this instance?

Mr. **Ferris**. I might question that premise, that it is a violation of copyright law to do that. It would not be economically wise to do it, instead of buying another book, but I think if I copy a book at home for my personal use, to mark up because I am going to make an analysis of it, or whatever I am going to do with it, I do not think that is a violation of copyright law. I think the notion that I can buy a record, but cannot go home and put it in the format that makes it more convenient for me to listen to that record, I think that the record industry fails to understand that the hardware manufacturers are the best friends that the software people have. Each time a new technology comes out they can go back and redo their entire catalog of offerings in another format and sell them again.

Senator **Metzenbaum**. Can somebody give me a better answer?

Ms. **Foreman**. Senator, I will try. I think that what we are doing adds to the income of the industry. I do not spend a lot of time at home where I can sit and listen to records, but I run almost every day. I bought three records last month, records I never would have bought to sit and listen to at home. I took them home and taped selections from them, put them on a 90-minute tape, that I can put in my Walkman and go running with.

Now, the selections I wanted were not available to me on prerecorded tape. Nor was I able to buy a 90-minute prerecorded tape. I would not have bought those records if it were not for my ability to take them and put them in the order, in the timeframe, and into the mode that was useful to me. The recording industry got money from me they would not have had otherwise.

To say that we cannot take a record and tape it is like saying you can read your book at home, but you cannot sit on the beach and read it, or you cannot loan it to your mother after you read it.

Senator METZENBAUM. Anybody else want to add to that?

Mr. FELDMAN. Neither could I have bought that same material in the quality level that I can record it from a recording at home, because the fact of the matter is that most prerecorded cassettes, up until very recently, have been of extremely poor quality, due primarily to high speed duplication, which does not permit the recording the kind of quality that can be done on a one-by-one, or in a real time basis.

Senator METZENBAUM. Are you saying that a copy of a cassette can produce better quality in some instances?

Mr. FELDMAN. No. I am saying a copy of the same material bought on a prerecorded cassette will not be as good as one recorded at home.

Senator METZENBAUM. I would like your opinion as to what are the problems that the way the bill provides for dividing up royalties. Are there to be Government regulations applicable to this division—as Mr. Gortikov suggested?

Mr. FERRIS. Senator. I think that is one of the real, and most significant weaknesses in the legislation, how moneys are going to be distributed. The only way we heard this morning from the recording industry is that it is going to be either by the record sales that will go to the rich artists, or is it going to be through some monitoring mechanism that we would monitor how people tape in the home. I have grave concerns about monitoring home taping; and I certainly found the statement of what the record industry thinks might be a solution—to include subliminal messages in tapes. I thought I was listening to Chairman Gorbachev. That is a very worrisome thing.

Senator LEAHY. We could see the worry on your face. I did not know if you were going to be able to continue today. [Laughter.]

Senator METZENBAUM. Is not the solution of this problem to do something about the dual recording devices? Are not these machines the source of much of the copying?

Mr. FELDMAN. Sir, I believe that these dual recording devices, as all recorders, serve a very specific need that the manufacturer—that the hardware manufacturer perceives, specifically the ability to have a longer playing time on a continuous basis. For example, the new compact disc allows as much as 74 minutes on a side.

Now, if I did want to take that to the beach in the form of a cassette, there would be no way I could record the entire disc on one side of one cassette, such that I would then have to stop the music, turn it over, and so on.

By having these dual-well cassettes, we have enabled a longer continuous playback time. That was the primary goal, so that you do not have to constantly keep flipping cassettes back and forth.

Senator LEAHY. Mr. Feldman, you do not really think—I have got two teenagers and a 21-year-old, and I see all their friends. You do not really think that they buy the dual cassette machines just so they can listen to a longer playing tape, do you?

Mr. FELDMAN. I think some of them are doing it for copying only.

Senator LEAHY. I think you could find one or two who could find somebody who copies. Do not leave us with the impression that that is the sole reason that they are there.

Mr. FELDMAN. I do not say it is the sole reason.

Senator LEAHY. Or even the primary reason.

Let us go back to the question I asked before. I wonder, Mr. Ferris, if I could begin with you. Suppose I hear a record I like at a friend's home and I think it is a good one. I do not want to go and buy it, but I sure as heck want to listen to it, and I bring it home and I tape it. There isn't any question of whether my taping equipment will make a better recording or a worse one. I have just taped it for myself so I can listen to it. Do I have any obligation or should I have any obligation to compensate the people who created that record and the music on it?

Mr. FERRIS. I think your question gave the answer. You said you brought it home and taped it because you would not go out and buy it. The fact is that destroys the myth of a displaced sale. What you are going to do, you are going to be able, if you tape that, to have this artist in your home so you can listen to it, or in your Walkman so you can listen to it. I think that is not a displaced sale, and I think——

Senator LEAHY. I think you misunderstand the emphasis of my words on that. I have got it here, so I do not have to go out and buy it. It is a record I really like. I have got one or two options. I can either buy it or borrow it. If I cannot borrow it, I have to go buy it, and I want the record.

Mr. FERRIS. I think the percentage of those events that take place as you described it is certainly a small minority, where you borrow it and copy it; but I still, in that case, do not think that it is an economic rein on the composer and the authors and publishers.

Senator LEAHY. You do not think the musician who wrote and performed the work should be paid for his work?

Mr. FERRIS. They are paid when the initial record is sold. I think the wider dissemination of that product is probably going to encourage more interest in an artist that might not otherwise get purchased. That is the synergy in this whole relationship between home recording and record sales. I think that is the failure of the recording industry to recognize that there is this very positive synergy between home taping and record sales. If somebody goes out and buys a record, because they wish to listen to it with a Walkman or at the beach, I think——

Senator LEAHY. What about the case of a person, say, with a group of friends? I hate to pick on teenagers, because it happens, certainly, in other age groups, but where one kid buys a record, the latest one out, goes over to a friend's house and they spend the whole afternoon making tapes for their own use.

Should the musician who performed that music be paid for his or her work, or do you see that as part of the synergy that one purchase makes it worthwhile?

Mr. FERRIS. I am wondering if each teenager who buys a record in that group of 10—and thus there are 10 sales—would even overcome their personal threshold to buy any single record, let alone to buy all 10 recordings.

Senator **LEAHY**. So the 10 sales instead of 100 justify it?

Mr. **FERRIS**. I think Mr. Graves might answer this question, because he has the personal experience as a retailer.

Senator **LEAHY**. Mr. Graves, what if I hear a record at a friend's home in East Barre, VT, put together by a good Vermont group, called the Throbulators—there is one by that name. I hear it and I like it and I borrow it, and I make a tape of it for myself. I do not want to go down to your store and buy the record album. Should I pay for the use of that music?

Mr. **GRAVES**. I think the thing here is you are being introduced to new music, and you will eventually buy more music, because you have all of a sudden been introduced to a new group or new sound.

Senator **LEAHY**. Let us say it is people I have heard many times before. Let me use this example. I have heard an artist, and we are getting more and more Vermont artists, and we are getting some pretty sophisticated and good recording companies in Vermont. If I have heard the record played many times on the radio, and I am at a friend's home, and he has got it, or she has got it, and I borrow the record and tape it myself, do I owe anything at all to that musician?

Mr. **GRAVES**. I do not believe so. I sell both blank tapes and prerecorded records and tapes, and when anybody comes into the store and they pick up a blank tape, and they head over to the prerecorded rack and they pick up one or two prerecorded tapes, you have got to have a balance.

Senator **LEAHY**. Would it surprise you to hear that the recording companies in Vermont would disagree with you?

Mr. **GRAVES**. I know of a recorder who disagrees with this bill.

Senator **LEAHY**. Would you be surprised if I told you that there are artists and recording companies in Vermont who disagree with the position that you have taken here?

Mr. **GRAVES**. Would it surprise me?

Senator **LEAHY**. Yes.

Mr. **GRAVES**. No.

Senator **LEAHY**. I have just one technical question. Am I correct that there is no home recording device that can make a CD?

Mr. **FELDMAN**. That is correct, but there may be one available someday.

Senator **LEAHY**. Is there one in the works?

Mr **FELDMAN**. Yes. Many laboratories are working on that today.

Ms. **FOREMAN**. I think we ought to acknowledge that there is some taping that displaces sales. Your friends who took the record and taped it because they liked it but did not want to pay for it exist. But I think the points being made here in rebuttal are not points that should be disregarded.

Senator **LEAHY**. Nor do I.

Ms. **FOREMAN**. You have identified a problem. I do not see anything in S. 1739 that addresses just that group of people. It assumes that each taping displaces a sale, and deprives the artist of something, and I do not think you agree with that.

Senator **LEAHY**. No. In fact, there are a lot of tapes that I use in my dictating equipment, for example, that I would never use to record music because the quality is too poor, so there should not be a royalty on them. I think there is a lot of displacement, and it concerns me greatly, and I am not going to be so unscientific to just use my own neighborhood or my children for an example, but I see so much of it going on that it does concern me. I do not think this bill is perfect by any means, or that the amount of royalties discussed are the proper amount, but I really hope that there is some way that we can work out something. We don't want to bankrupt the Tandy Corp. or Hitachi or Sony, or to have the yen fall apart, or anything like that. But there should also be a way to compensate artists. The example you used about Michael Jackson was a good one. But the people he bought it from are being compensated for their creative work, at least a number of them are.

So I hope there is something that can be done. These are hard questions, and I would strongly recommend to anybody that has views on this, both pro and con, to send them on to me and the chairman. We are still a long way before this is going to go through the Senate and the House, but I think that the issue may not be quite as black and white as both sides would tend sometimes to portray it.

Senator **Mathias**. Thank you, Senator Leahy.

Mr. Graves, while it is fresh in my mind, let me just follow up on a statement you made. You said you did not see any difference between the tape carrying music and the blank tape.

Do you think that an artist adds anything of value to a tape?

Mr. **Graves**. The artist?

Senator **Mathias**. The singer, the musician, whoever has recorded the work of art on to the tape.

Mr. **Graves**. To the tape that the consumer would be buying ultimately?

Senator **Mathias**. Yes.

Mr. **Graves**. It depends on the hardware. I do not understand what you are trying to get at.

Senator **Mathias**. You do not concede a work of art in sound has value.

Mr. **Graves**. Of course, it does, but he is being paid for that.

Senator **Mathias**. Mr. Ferris says that the musician is paid for his work when the recording is made, and that is the end of it. It appears to me that you agree with him.

Let me go back to an analogy of book notes. In the early days of book notes, in the days when Shakespeare was writing, you did get paid just when you took your manuscript into the printer: you got paid 5 pounds, 10 guineas, and that was the end of it. You had no expectation of any further payment, and if it was a runaway best-seller, it was the printer that made the profit—not the author. The inequity of that was perceived over a period of time by writers, by the general public, and even by the printer, and so the system of royalties came about. Thereafter, the creator or artist could be compensated in some proportion to the marketability and popularity of his work. Thus, when you make a recording, or when you write a book, you cannot be sure that you have got a hit. But you can be sure that you get paid something for your efforts through each writing or recording that is sold.

Now, if it is a great hit, should you not be compensated a little more than if it is a dud?

Mr. **Graves**. I think it depends on the contract they are signing.

Senator **Mathias**. Well, let us leave contracts out of it for a moment. Let us talk about a matter of human equity. Should you not expect to get more out of a hit than out of a dud?

Mr. **Graves**. Well, sure. Would not anybody feel that way?

Senator **Mathias**. That is all we are talking about. Senator Leahy is exactly right, we do not claim any special wisdom on this subject. In fact, we may know less than anyone else in the room about it. However, we are trying to devise a way by which the artist who has created something new, who has added something of value to that blank page or that blank tape, can be compensated in an appropriate way and not be cheated by a technological gimmick which makes it possible for others to get the benefit of his work by simply appropriating the value that he has brought to a blank page.

Now, how do we do that? If you have better ideas than we have, for goodness sake, let us have them.

Does anybody want to volunteer?

Mr. **Ferris**. I will volunteer, Mr. Chairman, but this might be repetitive. I think the examples that Senator Leahy and Ms. Foreman raised are useful. There are people who make tapes for many purposes. There are teenagers who make tapes of prerecorded music. But they are a small segment of a much larger picture. The synergy between the hardware manufacturers and the software manufacturers is not insignificant. The testimony this morning talked about the nature of the revenue split between the artist and the record company. And that split is going to depend on how much leverage each side has. The little artist that comes in is going to be like Shakespeare. He is going to get his 10 guineas and go home, and if it is a hit, he will have some leverage next time. But I want to reemphasize that all of this new taping hardware has provided a tremendous profit opportunity for the recording industry, and yet another opportunity. The compact disc is going to provide an additional revenue stream for the recording industry.

You have heard the dire predictions before this committee many times. In the early fifties, the Hollywood studios felt that television was a threat; and then cable television was perceived another threat when it came on stream in the last sixties. But these new distribution streams were not enemies but very profitable, new distribution opportunities. They turned out to be friends, and very profitable friends. So, too, in this case!

Senator **Mathias**. Maybe this will bring us back to the question I posed to Ms. Foreman. What is it that the copyright seems to do? A copyright is not intended by the Constitution nor the enabling statutes to guarantee income to anybody. It is to protect property right. It has the same function as a deed has to your house. It is evidence of your right to control certain property. That is all that does, and that is all that I see that the legislation should intend to do.

Ms. **Foreman**. Senator, while you were out of the room, I said some of the things I am going to say again. I agree with you, it is a balancing act. One of the things that troubles me is that your bill does not in any way take care of a particular issue that I have raised. I like to listen to a tape while I run. I buy records that I would not ordinarily purchase in order to tape selections from those records, put them on a tape that is longer than any prerecorded tape that I can buy, and of a higher quality than any prerecorded tape that I can buy, so that I can take it with me while I run or while I work.

Surely the industry does not believe that I should have to pay a penalty to listen to their music in the order that I prefer rather than in the order that they have chosen to record it. Nothing stops me from getting up and going across the room and picking the arm of the phonograph up and moving the arm over to another selection. I am not depriving the artist when I do that, and I am not depriving the artist when——

Senator **Mathias**. And, granted, we catch you in the net while trying to protect the artist.

Ms. **Foreman**. You certainly do, and my concern about the bill is that it penalizes us for an appropriate use of copyrighted material. Further, and I do not think there is a thing in your bill that says that the money is going to go back to the artist. You write a bill that says there is absolute security that a starving artist is going to get the money, and I will pay the tax.

Senator **Mathias**. Well, of course, that goes back to the question that I put to Mr. Graves about what kind of contract they signed. Obviously, if an artist signs away all his copyrighted interest to a publisher, that does affect his ultimate recovery. But if he retains rights to some portions of the royalties, then no matter how obscure an artist he is, he will benefit.

Ms. **Foreman**. It is my understanding that the overwhelming majority of artists who participate in any recording do so for a flat fee. They are paid a session fee. They do not get any royalties at all. So royalty money tends to go to a very elite group among artists, and primarily to the owners of the copyrights who are not the artists, but the recording companies.

Senator **Mathias**. Well, we will ask for some information with respect to the customs of the trade so that we can better assess that issue. But if in fact there was a hope of collecting royalties for the musical recordings being copied without authorization, it might alert artists to be more diligent in protection of their own rights. In any event, the equities of the case are clear.

Mr. **Feldman**. Senator, I think there was one point. Unfortunately, Senator Leahy had to leave the room, but he stated he would not use the grade of tape that he would use for material such as music, and this precisely raises one of the fatal flaws in the proposed bill as presently written. Specifically, that is exactly the type of inexpensive, lowgrade tape that the teenagers that he was worrying about were using to make those copies that he was concerned about.

Now, those, apparently, ostensibly, would not be taxed in any event; whereas, the high grade that Ms. Foreman plans to use for a legitimate purpose would be taxed. So there seems to be no way of differentiating, as I pointed out in my earlier testimony.

Senator **Mathias**. In your written statement, you say that tape cannot be classified according to use. Is that correct?

Mr. **Feldman**. That is correct.

Senator MATHIAS. But it says any generic type tape may be used for recording purposes. Would that not be inconsistent with what you just said?

Mr. FELDMAN. No, sir. I am saying the measure of quality is in the minds of the listener. The teenager, because of financial restraints, might be perfectly content to use the lowest grade tape to record music, and this is apparently what they will do because of their economic need. It will record the music, but it will not record it in the highest quality sound, but nevertheless would serve their purposes, and that would be a tape that the bill would not tax.

Senator MATHIAS. Well, of course, you understand the reason we impose a royalty on some tapes and not others. Whenever the Congress enacts a general law for a general purpose, we have a very difficult time distributing the impact of that law equitably among all the population.

Ms. FOREMAN. Senator, the industry had record sales last year. It is hard to make the argument that they are in a position where they are suffering seriously. It is hard to make an argument that the industry is suffering seriously when they had record sales in 1984 and are heading that way again in 1985. Is it appropriate for the Congress to enact a very broad law that catches a lot of people who are not in any way doing anything that is inappropriate in order to compensate artists, when injury really has not been shown.

Senator MATHIAS. The Congress is attempting to make this as narrow as possible, and we are doing so relying on the situation we are seeing in the marketplace. Now, just as a coincidence, we have this poster right before us. This is one tape manufacturer's guideline as to what kind of tape you ought to use for what purpose. On the left-hand side there is the kind of music and on the right-hand side there is the tape you ought to use.

Maybe we ought to be a little more precise in our own definitions, but orchestral and operatic music, digital disc or master tape, appear to require one kind of tape. That is the way you in the industry are marketing these things, so we are trying to respond to the kind of signals that those in the marketplace are conveying.

Mr. FELDMAN. Sir, if I were a tape manufacturer, that is the way I would advertise tape as well.

Senator MATHIAS. You mean the Congress should not believe you?

Mr. FELDMAN. That is a good advertisement, if one has the funds to respond to that layout of tape classifications, but, as I mentioned already, the lowest grade on that chart will record music quite nicely.

Mr. BATTAGLIA. Senator, if I may, we are in a very high technology, fast paced industry. It is 10 years ago, 1975, we used our premier state of the art of Ella Fitzgerald singing and shattering a glass. Today every tape can shatter a glass. Technology moves that quickly.

So a state-of-the-art segment of tape would be the benchmark by which we will measure.

Senator MATHIAS. I acknowledge that the technology moves faster than the Congress. Charlie Ferris will recall the 1976 copyright act. We thought we could be like the Lord. We had reached the seventh day and we could rest. We even disbanded this subcommittee. Then, we found out that technology moves so fast that we had to reconstitute the subcommittee, and we know that we are out in a pioneering area, that we are trying to find ways to protect intellectual property values in a technological field for which there is no precedent. We are trying to explore the various new problems that confront us.

America has a tremendous interest in this because more and more we are turning from a production nation to a service economy. That means we are selling ideas, we are selling intellectual property in the world marketplace, and if we do not find ways to protect that intellectual property, we are going to have a tougher and tougher time.

I am not just talking about the music industry or entertainment industry, but they mentioned floppy discs and other computer technology. All of this is going to be exposed to various kinds of piracy. I use the word not in a technical sense, but in a commonplace sense. America has a vital interest in advancing the protection of intellectual property and respect for intellectual property; whether this bill embodies the proper application, we need the advice and counsel of you leaders in the industry in order to protect this critical American resource: Intellectual property.

Ms. **Foreman**. Senator, in a field that is changing so rapidly and at a time when the recording industry's figures really reflect only what happened during a period of enormous recession, when every business in the country was seriously injured, would it not be better to wait a little while, see how the industry rebounds from the recession, see what the impact of the compact disc is going to be on the industry.

I may have to go and replace my whole record collection, and I think the industry is going to make a bundle of money out of that. Maybe this is not a very good year to address this problem. The Congress perhaps ought to hold back a little bit.

Senator **Mathias**. Let me ask this question, or maybe I should ask Mr. Feldman. Do you think that technology is going to slow down?

Mr. **Feldman**. No. I think it is going to accelerate.

Senator **Mathias**. That is what I think, and I think we will get further behind the curve the longer we wait.

Mr. **Feldman**. I think that technology will yield further profits for the entertainers and the industry. They sort of work hand in hand.

Senator **Mathias**. I hope you are right. And I have no reason to believe that we will not see that prediction bear fruit, but there is also a question of equity here. Property rights are property rights. I suppose you could say it does not matter so much if you steal a poor man's cow or a rich man's cow. It does not make any difference if you steal the car of a man who is making $10,000 or $1,000. There is really a question of equity here. Are we dealing with someone's property? Hasn't society reached the point where an idea is viewed as a piece of property?

Clearly it is, if you write it down on paper and have it printed in a book and copyright the book. That is the kind of threshold we are trying to cross here.

Mr. BATTAGLIA. Senator, we have a bill as a tax on tape.

Senator MATHIAS. All tape that exceeds a certain quality threshold.

Mr. BATTAGLIA. I think it is very broad and encompassing. I believe that we are making an assumption that each of these tapes that can be taxed displaces a sale at the moment it is used—a sale that would benefit the recording industry. I do not believe that to be the case. I believe the majority of the blank tapes, the vast majority of blank tapes, are used in the application that Ms. Foreman said. One records their own record collection for use in a specific way that a record company is not providing the material. The record industry does not offer these options—provide these options.

However, the record industry does not feel that they are getting sufficient reward to the artist involved at the point of the original sale. Maybe that is the best place to go after the compensation for the artist.

Senator MATHIAS. I hear what you are saying, and I can comprehend that there are, as the Supreme Court recognized in the *Betamax* case, some legitimate reasons to tape.

I wish we had a perfect solution and am interested to hear what you propose as alternatives. We will keep the record open for 30 days, so if you want to sleep on it and come up with some ideas, you can let us know.

Let me ask you one last question.

The Register of Copyrights has testified that many countries have passed laws in recent years which address this home taping problem. This is not a problem which is unique to the United States. There are other countries that face the problem and have done something about it. They have passed laws similar to that embodied in S. 1739. There are others who are in our position; they recognize the problem, but they have not found a solution. Did those who have passed this type of legislation make a mistake?

Are you aware of the experiences in any of those countries?

Mr. FERRIS. Mr. Chairman, I am certainly aware of the activity overseas, especially in Europe, and there is no doubt that the balance between the consumers' interest and the proprietary interests are going to be resolved differently in each country. I think we should not always rush to judgment that what they do is right and what we do is wrong. I think the balance between the copyright holders and the users—the consumers—that is reflected in our existing copyright law has created the environment where we create more artistic product than in any European country or even all combined. I think our environment is the most optimum environment, and before we change it, we should really reflect to see if what we have is really wrong. I do not think it is.

Senator MATHIAS. Well, you may be right, Charlie. I wonder: If we had a time machine and we could go back in time to a period before property rights and domesticated animals, I will bet people were arguing that anyone could milk a cow. The first one who got to her could milk her, and anyone was entitled to her milk.

Mr. BATTAGLIA. Senator, I have some firsthand experience. I lived in Germany for a couple of years, and I managed our tape business in England, and I lived in England. I think that each of these countries that have these types of access for the consumer and these items is not pleased with the results. I do not believe that they achieved their objectives, and I think we should think seriously about——

Senator **Mathias**. Is that the point of view——

Mr. **Battaglia**. I am speaking for mostly the consumer. I was managing our Memorex business in Germany and gained my experience there in that capacity, and I then managed it in England. I think the people would like to change it.

Senator **Mathias**. Obviously, we have not completed our investingation into this subject. There may be additional questions that members of the subcommittee would like to ask of you. I would appreciate it if you would be willing to answer those questions and your answers would become part of the record. Your full statements will be included as part of the record. We will keep the record open for 30 days for additional questions, answers, and comments. If anyone wakes up from a dream some night and comes up with a perfect solution, hurry down—we are waiting for you.

Thank you very much.

[Whereupon, at 12:55 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

HOME AUDIO RECORDING ACT

TUESDAY, MARCH 25, 1986

U.S. Senate,
Committee on the Judiciary,
Subcommittee on Patents, Copyrights and Trademarks,
Washington, DC.

The subcommittee met at 9:40 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Charles McC. Mathias, Jr. (chairman of the subcommittee), presiding.

Also present: Senators DeConcini, Metzenbaum, and Specter.

Staff Present: Steve Metalitz, chief counsel and staff director; Matthew Gerson, counsel; Pamela Batstone, chief clerk; Diana L. Waterman, Judiciary general counsel; Beverly McKittrick, counsel to Senator Laxalt; John Podesta, minority chief counsel; Eddie Correia, counsel to Senator Metzenbaum; Ed Baxter, counsel to Senator DeConcini; and Scott Green, counsel to Senator Biden.

OPENING STATEMENT OF HON. CHARLES McC. MATHIAS, JR., A U.S. SENATOR FROM THE STATE OF MARYLAND

Senator Mathias. The Committee will come to order.

The Subcommittee on Patents, Copyrights and Trademarks convenes this morning for further consideration of Senate Bill 1739, known as the Home Audio Recording Bill. This legislation would legalize the home taping of copyrighted music and other audio materials but it would do so in exchange for a modest royalty on the tools used to make the copies. It is intended to be a measured response to the overwhelming evidence that advancing technology is impairing the effectiveness of the copyright law.

As many of you know, the subcommittee conducted a hearing during last fall that generated an expansive discussion of this approach to solving the home taping problem. Today, we have asked the industries that would be most affected to focus on two issues presented by Senate bill 1739. The first is whether technology, which has, after all, created this problem, might be able to solve the problem that it has created.

Some years ago, I was in Bangalore, India, and visited the Indian Institute of Science. The director, who was a very able and wise man, said that the proper solution for problems created by technology is more technology. So we will test that thesis this morning.

I am not going to attempt to explain all of the gizmos and notches and frequencies that are involved in a technological solution. That is why the witnesses are here, to tell us. I would, however, point out that if compatible components are placed into sound recordings and recording devices, consumers will not be able to copy copyrighted material simply as a matter of course. So the record companies would then be in a position to distribute a copyable recording for the home taping enthusiast, and then offer, presumably for a different price, some which would not be susceptible to being copied.

I would like to emphasize that Senate bill 1739 does not require those who manufacture the audio recording devices to include in their equipment the decoder that will be demonstrated here this morning. Instead, it provides that the manufacturers will have the option of paying the royalty on machines, or avoiding the royalty by including a decoder. It fosters a marketplace solution so that only those who tape are those who pay for the privilege of doing so.

Of course, this technology is brand-new. Congress has never before looked at this method of protecting intellectual property. And while I welcome the scrutiny that an idea like this deserves, and I trust that we are going to learn that, as is said, "All that glitters is not gold," I cannot help but be intrigued by a technological solution to this home taping problem, a problem which has proved to be a difficult political and legal one. American copyright law has often evolved in response to technological developments. Congress has usually found itself playing catchup to the new technology. We will ask today's witnesses whether, in this instance, the inventors will work with the Congress so that copyright holders will not be harmed by the home taping phenomenon. This is an opportunity to bring the law and inventions into sync.

The other issue that this hearing will address concerns the distribution of royalties that would be generated by the legislation. S. 1739 was introduced to ensure that the creators and the producers of America's music receive fair compensation for the home taping of their works. After all, the underlying premise of the constitutional authorization for copyright legislation is to provide artists and authors and other creators with an incentive to develop their talents so that the general public can benefit from and enjoy their creations. The home audio recording bill rests on the proposition that the short-term gain to the consumers from unrestricted home taping is outweighed by the costs that the whole society ultimately will have to pay if America's rich and diverse musical tradition is in some way injured or damaged.

Many have questioned whether we can be certain that this legislation will achieve the goals of protecting America's music. Their skepticism has focused on whether the record companies would actually use the royalties to cultivate new recording talent. The people that we have heard from wanted some assurance that lesser known or less established performers—including many of the classical, jazz, folk, and gospel artists—would be well served by our efforts.

The subcommittee has asked the recording industry to confront the royalty distribution questions and to present some sort of a plan that would respond to these legitimate concerns.

So, without taking more time, I am hopeful that today's hearing will illuminate at least these two issues, and will allow us to move ahead to a markup in the very near future on Senate bill 1739.

Our first witnesses this morning will be Mr. Stanley Gortikov, a veteran performer on this particular stage, president of the Recording Industry Association of America, and Donald McCoy of the CBS Technology Center.

Gentlemen, we ask you, as I will ask all witnesses, to keep your remarks as brief as possible. Any part of your statements that you do not read we will include as part of your statement in the record.

Thank you.

STATEMENTS OF PANEL CONSISTING OF STANLEY M. GORTIKOV, PRESIDENT, RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC., NEW YORK, NY; AND DR. DONALD S. McCOY, GENERAL MANAGER, CBS TECHNOLOGY CENTER, STAMFORD, CT

Mr. Gortikov. Thank you, Mr. Chairman.

Today we seek legislation to respond to the technological problem of home taping. This time we come with a technological alternative that allows the marketplace to determine the appropriate response to home music taping. With this new technology, which we will demonstrate shortly, copyrighted records, tapes, or compact discs can be encoded with an inaudible code that sends a signal to a special electronic decoder which would be installed in future generations of audio recorders, that would either permit or inhibit the copying of that particular recording. This decoder technology is anticipated in S. 1739, the Home Audio Recording Act.

The legislation specifically exempts from the payment of royalties all audio recording machines equipped with such a decoder. Until now, that exemption has been largely conceptual but, today, we demonstrate that copy-coding, as we call it, is a reality. And to describe that technology, I am pleased to introduce Dr. Donald McCoy, vice president of Technology of CBS, Inc.

Senator Mathias. Dr. McCoy.

STATEMENT OF DONALD McCOY

Dr. McCoy. Good morning, Mr. Chairman.

I am Dr. Donald McCoy, vice president of Technology for CBS and General Manager of the CBS Technology Center in Stamford, CT.

With me this morning are my colleagues, Emil Torick, David Stebbings, and Krystyna Vaughan from the CBS Technology Center.

Senator Mathias. We are happy to have them here with us today.

Dr. McCoy. It is our honor to appear before you today to describe and demonstrate the CBS copy-code system.

The copy-code system begins with this electronic device, the encoder. It removes from the master recording a tiny sliver of sound, of sound energy from the upper middle portion of the audible sound spectrum at a frequency beyond the fundamental tone of the highest note of any musical instrument. The change caused by the encoding process is effectively inaudible and does not affect the quality of the music.

In other words, listeners cannot distinguish the encoded recording from an unencoded recording.

To demonstrate, let us play the same brief segment from a familiar Barbra Streisand tune, once from an LP that has been encoded and once from an unencoded LP.

Krys.

Senator MATHIAS. Which is first?

Ms. VAUGHAN. This one is conventional.

Senator MATHIAS. So this one would be subject to being copied?

Dr. McCOY. Yes.

Senator MATHIAS. I do not know how the reporter is going to be able to transcribe this segment of testimony. [Music played].

Dr. McCOY. All right.

Now we will play the other segment, the encoded version. Sorry that the sound level is a little low there. We are operating without a pre-amp that failed to make its appearance this morning. [Music played].

All right. Let me show you that even trained observers have not been able to detect reliably which album was encoded and which was not.

As we said, from the test we just conducted, the first play was in unencoded form and the second was from the encoded version.

Now, although our human listeners cannot tell that these two albums are different, a cassette recorder equipped with a decoder, the other component in a copy-code system, can make that distinction and do it reliably time after time.

The decoder, which we call a copy-code scanner, is an integrated circuit chip designed to be built into the recording mechanism of future models of audio recorders.

When a record is taped, the decoder scans the music, looking for the encoded notch where the sliver of sound was removed. When the decoder detects the notch and locks onto it for a number of seconds to assure that there is no mistake, circuitry within the scanner chip inhibits the recording function for a period of 25 seconds. The cycle is then repeated.

If the scanner determines that the notch is still present, the recording function is interrupted for another 25 seconds. An attempt to tape a program from any source that is protected by the copy-code signal will therefore consist of brief segments of recorded program, but they will be interrupted periodically by 25-second dead bands without sound.

This recording machine at the end of the table is equipped with a scanner of the type that I have just described. It will make a normal recording of any album that is not protected by the copy-code notch. The scanner will simply scan the music, determining that there is no notch, and permit copying.

When the music has been encoded with a notch, however, it will be detected and the recording will be interrupted.

To demonstrate, we will insert a new premium music quality blank cassette into this recorder and attempt to copy the encoded album you just listened to. [Music played.]

And note that there is a small red light in the upper left-hand corner of the recorder. That will come on when the scanner has detected that it is trying to record copy-coded material. And at that point, the recording function will be disabled. [Music played.]

Senator MATHIAS. The sound never dies out totally?

Dr. McCoy. In this playback mode, you are hearing the music as it comes straight through. We will play that tape back for you and you will find that it has stopped recording at that point when the little red light went on.

Senator Mathias. I see. We are still in the recording process, we are not in the playback process.

Dr. McCoy. All right. Now we will rewind that tape and show you the point at which the recording was stopped. The recording was disabled, and you can see that the sound level is reduced to the point where it would be unusable.

Senator Mathias. And that blank period lasts for 25 seconds?

Dr. McCoy. It lasts for 25 seconds, and then the scanner again checks to see whether the copy-code is present.

Senator Mathias. And how soon will the 25-second interruption occur?

Dr. McCoy. On the average, it takes from 13 to 20 seconds for the scanner to determine that a copy-code is present. It could be done shorter than that, but we have sort of bent over backward to make sure that it will not make a false identification.

Senator Mathias. What is the interval between the interruptions?

Dr. McCoy. In a typical case, it will record for something between 13 and 20 seconds, go off for 25 seconds, come back on for 13 to 20, go off for another 25 seconds, and that process would repeat as long as you were trying to copy any copy-coded material.

Senator Mathias. So, essentially, it would produce a repeatedly interrupted recording that is hardly worth listening to.

Dr. McCoy. I think with interruptions of that sort, it would effectively eliminate the value of the recording. And the same thing will happen whenever an attempt is made to copy music from an encoded source on an audio recording device equipped with the scanner, whether that encoded source be a record, a prerecorded tape, a compact disc, or a radio broadcast of any such protected source material.

The concept of the copy guard notch can be extended to any audio recording device that may be developed in the future.

Copy-coding technology is ready for implementation. The encoding device before you is ready for manufacture. The circuitry in the scanner we have here is presently being designed in semiconductor chip form and will be available within a few months for sampling to the industry and for mass production.

An important aspect of our copy-coding solution is that it is inexpensive. The decoder chip is expected to cost less than $1 when produced in large volume. If manufacturers of audio recording devices are able to develop compatible circuitry that can perform the same functions more efficiently or at lower cost, they would be free to do so so long as they will reliably inhibit the recording of copyrighted material and are not easy to circumvent.

In any event, we at CBS, in recognition of the important benefits that the system will provide to all copyright beneficiaries, have pledged to license both the encoder and the scanner that we have developed on a royalty-free basis for all hardware and software applications.

[Prepared statement of Dr. McCoy follows:]

PREPARED SUMMARY STATEMENT OF DR. DONALD S. MCCOY

The copy-coding system, developed by audio engineering experts at the CBS Technology Center, has two elements: the encoder and the decoder.

The encoder is a small electronic device that can "encode" any master recording (whether in digital or analog form) by intermittently removing tiny slivers of sound high in the frequency spectrum (beyond the highest notes of any musical instrument and between the notes of the musical scale). To create this "notch" in the frequency spectrum, the recording is simply passed through the encoding device electronically. The notch thus embedded in the recording is effectively inaudible and does not affect the quality of the music.

The decoder is an integrated circuit ("IC") or chip designed to be built into the recording mechanism of future models of audio recorders. When the recording mechanism is switched on, the decoder scans the music, looking for the encoded notch, which is present only in uncopiable versions of copyrighted recordings. When the notch is detected, the decoder inhibits the recording function of the machine for a period of 25 seconds. The cycle is then repeated; if the scanner again determines that the notch is present, the recording function is interrupted for another 25 seconds. A copy taped from an "uncopiable" recording will thus consist of brief portions of music interrupted periodically by segments without sound.

Copy-coding technology is presently available for implementation. Encoding devices have already been produced and successfully tested, and are ready for manufacture. The circuitry for the copy-code scanner has likewise been produced and tested, and in the next couple of months it will be available for mass production in semiconductor chip form.

The copy-coding solution is also cheap: The decoder chip is expected to cost less than $1 when mass quantities are produced and equipment manufacturers are free to develop a compatible IC that can perform the same functions more efficiently or at lower cost. In any event, CBS has pledged to license both the encoder and the decoder that it has developed on a royalty-free basis for all hardware and software applications.

The principles of copy-coding can be adapted to all existing technologies and can be applied to all emerging formats as well. It is effective on every recording medium and method of electronic transmission. And it can be used on digital as well as the analog recordings.

Mr. GORTIKOV. The copy-code system that proves that the American creators need not be helpless victims of taping technology.

It is now clear that the same technical wizardry that has produced machines capable of copying our musical recordings can also produce devices to protect our musical recordings. And with the copy-code system, home tapers would still be able to reproduce our copyrighted music if they wish. They would simply be asked to pay for that privilege just as they already pay for the multiple copies of anything else they buy.

At present, the person who buys a prerecorded cassette for his own listening pleasure must pay the same price as the person who buys that cassette but then gives copies of it to others by using a high-speed dual cassette machine. Not so with copy-coding.

With this new technology, consumers can buy the type of recording they want. The purchaser who wants a single copy of a recording would buy an uncopiable version, one that is encoded. The person who intends to make copies would buy a copiable version which would include in its price compensation for the creators and copyright owners whose music is taped.

Copy-coding is strictly a prospective solution. Existing albums, tapes, CD's are not encoded and they can be copied on any recording device whether or not equipped with the decoder.

Similarly, any recording equipment now in the marketplace or in any consumer's home for the remainder of its useful life will be fully capable of recording from both encoded and unencoded music sources. That is why we need to continue to need royalty legislation, because it would be decades before copy-coding can make a significant dent in the home taping problem.

But the technology does offer something very important now, a way for the marketplace to determine the most appropriate response to home taping.

Under S. 1739, machines equipped with a decoder chip are exempted from any royalty. The Japanese equipment manufacturers therefore can make a marketplace choice either to utilize copy-coding technology or pay a royalty on their machines. Those manufacturers claim that their devices are not being used to tape our copyrighted music as indicated in this ad. The way they portray it, their machines simply enable people to record themselves playing the guitar or to tape class lectures or church sermons. If so, then there can be no objection to the use of decoder chips where the chips would not interfere with such uses. It would only enable us to protect our copyrighted recordings.

The only reason the equipment makers might choose not to install the decoder chips in their recording machines is so that their customers can take our prerecorded music without paying for it. In that case, it is entirely appropriate that they do pay an equipment royalty to those in the music community who are victimized by their practices.

Let us face it. The Japanese electronics and blank tape manufacturers will not voluntarily help the American music community. They have got a good thing going. They sell millions of machines, hundreds of millions blank tapes every year, designed and promoted so that their customers can own but not pay for the prerecorded music we sell.

Every statement they will present today will deny that there is any problem. That is why we need legislation enacted by Congress. They would have you believe falsely that the right to make multiple copies is included in the price of every recording. No matter how reasonable the choice we offer, the equipment makers will do nothing unless Congress acts.

For every album that is bought today, one is taped. Only Congress can mandate an end to that free ride that the tape and equipment manufacturers take on the backs of American creators. And for that we urge the enactment of S. 1739.

[Mr. Gortikov's submissions for the record follow:]

PREPARED SUMMARY STATEMENT OF STANLEY M. GORTIKOV

The manufacturers of blank audio tape and audio recording equipment design and market their products for the purpose of reproducing the copyrighted music we sell, displacing sales of our records. Because they profit from home taping, they should help those who are harmed by it. Thus, S. 1739 requires that royalties be paid on blank tape and equipment used for home music taping.

Exempted from those royalties are audio recorders equipped with "decoders." A system utilizing decoders would allow copyright beneficiaries to protect their copyrighted recordings and to receive compensation from those who copy them. Today, we demonstrate that such a copy-coding system is currently available, easy to implement, inexpensive and highly effective.

Copy-coding means that the American music community need not be a helpless victim of taping technology. With copy-coding, consumers can buy the type of recording they want: The purchaser who wants a recording just for his or her own personal use would buy an "uncopiable" version—one that is encoded with the notch, while a purchaser who wants to make multiple copies would buy a "copiable" version, the price of which would include compensation for the copy-right beneficiaries whose music is being taped.

Copy-coding is strictly prospective—it will not affect consumers' ability to copy existing albums, tapes and CDs, and they will be able in the future to use equipment now in the marketplace or already purchased to copy otherwise uncopiable recordings. It will, therefore, be decades before copy-coding can make a significant dent in the home taping problem. Accordingly, there is a continuing need for royalty legislation.

But, even in the near-term, the copy-coding system offers something very important—a way for the marketplace to determine the most appropriate response to the home taping situation. The Japanese equipment manufacturers can decide whether they prefer the copy-coding approach or the royalty approach. Under S. 1739, equipment makers can choose to pay a royalty or they can exempt themselves from any royalty by installing decoder chips in their machines.

If, as the equipment manufacturers claim, their devices are not being used to tape our copyrighted music, but are being used simply to enable people to record themselves playing the guitar or to tape class lectures or church sermons, then there can be no objection to the use of decoders. They would not interfere with those or any other non-infringing uses of audio tape recorders, but would only enable us to protect our copyrighted recordings.

The only reason manufacturers of recording equipment might choose *not* to install the decoder chips in their recording machines is so they can sell those machines for the purpose of reproducing our copyrighted music. And if they choose to profit by selling machines which enable their customers to take our prerecorded music without paying for it, they should pay an equipment royalty to those in the music community who are victimized by their practices.

In sum, the technology necessary to implement the "decoder" exemption in S. 1739 is now here, offering a fair, simple and efficient marketplace mechanism to respond to the problem of home taping.

Recording Industry Association of America, Inc.
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Stanley M. Gortikov
President

April 21, 1986

The Honorable Charles Mathias
Chairman, Subcommittee on Patents
  Copyrights and Trademarks
Judiciary Committee
United States Senate
Washington, DC 20510

Dear Chairman Mathias:

The following is my response to the questions you and Senator Specter submitted to me after your Subcommittee's most recent hearings on S. 1739, the Home Audio Recording Act. In the interest of providing thorough and concise answers to your questions, I have grouped together some of the questions posed and provided a single comprehensive response to those questions.

* * *

QUESTION

I am informed that CBS Records projects total retail sales for the U.S. recording industry in 1986 to be in excess of $4.52 billion. This represents more than 3.5% higher than 1985's estimated $4.37 billion. If the record industry continues to be profitable, then what reasons can it cite for the need to impose a royalty fee on tapes and recording equipment? Along the same lines, how can the "decoder chip" technology address this "problem" and do you expect record sales to increase in the near future?

RESPONSE

The projected modest growth in retail sales, even if borne out by the actual data, does not show that there is no home taping problem. First, and most fundamentally, the projection of retail sales is irrelevant because it does not reflect how many sales will be displaced or how much income will be lost because of home taping. In short, home taping is no less of a problem because the copyright beneficiaries deprived of compensation may happen, in any given year, to have a positive cash flow. Rather, it remains a problem because copyright beneficiaries deserve, like everyone else, to be compensated when their labor and property are used by others.

Second, contrary to the assumption reflected in the question, the level of retail sales tells nothing about the profitability of producers -- it neither measures income to record companies nor takes into account their expenses. Moreover, the real test of whether home taping is having a negative impact on the creation and dissemination of new music -- which is what the copyright laws are all about -- is not retail sales, nor even the profitability of record companies, but the number of new releases. By that measure, the harm caused by home taping becomes very clear: from 1978-1984, the number of new releases declined by nearly half. We are pleased to report that releases increased by 9% in 1985; nonetheless, the level of creation of new music remains substantially below what it was in 1978.

Finally, a word about the ARRC's reference to CBS Records' optimistic projection for 1986: One has to wonder why the ARRC refers to projected results in 1986 but say nothing about how the industry actually fared in 1985. The answer should be obvious -- the actual data show that record company dollar sales were flat in 1985, i.e., there was no improvement over dollar sales in 1984. Moreover, unit sales in 1985 declined 4% from 1984 levels.

Copy-coding technology will address the home taping problem by ensuring that copyright beneficiaries receive a measure of compensation whenever their recordings are copied. Regardless of how many records are sold in future years, copyright beneficiaries will continue to deserve compensation for revenues lost when their pre-recorded music is taped rather than purchased.

QUESTION

How much would it cost for a record company to purchase the machines that implant the encoder signal? I don't imagine that CBS would have any trouble affording it but what about the smaller labels?

RESPONSE

An encoding device such as the one displayed at last month's hearings would cost record companies approximately $2,000 as a one-time expense. Since the same encoder can encode all of a company's master programs, the capital outlay required is minimal and even the smallest commercial labels will be able to afford encoders.

QUESTION

If, because of competition for shelf space, the record retailer has to cut somewhere, prudent business judgment will be to stop carrying the artists and music forms that traditionally sell fewer albums. Doesn't that mean that this technology will be harming the less popular artists and music forms that this legislation is trying to help?

RESPONSE

Those opposing legislation that would permit the implementation of decoder technology should not be allowed to hide behind vastly overstated concerns about dual inventories. In fact, copy-coding should not result in any harm to less popular artists and music forms or indeed to any artists or music. Whereas retailers exercising prudent business judgment might now order 50 copies of a particular release, the prudent thing to do when copy-coding is implemented will still be to order 50 copies -- some of which are copiable and some of which are uncopiable. No less popular releases need be "squeezed-out." In other words, the need for dual inventory should not harm any retailers, consumers, record companies or artists.

In any event, if additional shelf space is desirable, retailers could reclaim some of the space taken up by the multiple inventory they maintain of blank tape. Retailers now stock numerous different brands of the same kind of tape, all of which are designed to do the same thing -- to enable purchasers to tape the pre-recorded music we create without paying for it. If anything has squeezed out less popular artists and music forms, it is the shelf space once used for music which is now devoted to blank tape.

QUESTION

Do you think that any labels might choose not to utilize the encoder device, and allow the consumers to continue to copy their music?

Should they be permitted to do so?

RESPONSE

It is quite possible that some labels might choose not to encode their releases, thus permitting copying of the records, tapes and compact discs they produce. If a record company and other copyright beneficiaries choose to follow this course rather than release both copiable and uncopiable versions of recordings, they should be free to do so. Indeed, one of the virtues of copy-code technology is that it permits competing record companies to make independent marketing decisions regarding what steps, if any, to take in order to protect copyrighted music.

QUESTION

How would you stop radio broadcasters from playing records which could be taped? Would you suggest that the Congress require radio stations to pass all their broadcasts through an encoder?

One way for a radio station to have an encoded signal is for it to play only encoded records over the air. Don't most radio stations get most of their record library free or at reduced cost from the record companies? If so, can't you exercise some self-help in this situation by making only encoded records available to the stations? Is there really a pressing need for a statutory requirement of an encoded signal?

Perhaps Congress should only require radio stations to pass their broadcasts through an encoder if the station is broadcasting a live concert. What is your reaction to that option?

RESPONSE

Radio stations should not be required to pass their broadcasts through encoders, but they should use encoded sources whenever those sources are available to them. Of course, they could choose to encode material such as live concerts which they originate. Such a decision to make a live broadcast uncopiable would be made by the broadcaster, or pursuant to contractual arrangements, by the orchestra, band or opera company which is being broadcast.

It is certainly true that record companies can exercise "self-help" by providing only uncopiable versions of releases to radio stations. However, such self-help is of limited utility if radio stations intent on facilitating home taping by their listeners could simply purchase unencoded versions of music in their local record stores and then broadcast these copiable recordings.

At this point, it is too early to tell whether a statutory obligation must be imposed on broadcasters to play only encoded records when such sources are available. We must first await the decision of the marketplace, to determine whether the Japanese manufacturers of audio recording equipment choose to adopt the copycode system. If the manufacturers elect to pay the royalty instead, then a statutory requirement of an encoded signal will not be necessary.

QUESTION

Mr. Gortikov, in previous hearings you have alleged that many people get together to buy one prerecorded album or tape and then make additional copies so that each contributor gets his own copy. Once the price of the copyable album increases, won't you encourage just that type of behavior? Maybe people would even get together just to pay the royalty on an audio recording device without a decoder.

ANSWER

Of course, the music community would prefer to see no sales displaced because of home taping. We realize, however, that such displacement does occur, and that copyright beneficiaries are deprived of significant revenues because of it. The music community, therefore, supports implementation of copy-coding technology and tape and equipment royalties because they would provide copyright beneficiaries with a measure of compensation for home taping. It would be regrettable if adoption of these measures resulted in an increase in home taping; at least, however, we will receive some compensation for that taping, which is presently denied us altogether.

QUESTION

You observed that the encoder is a totally prospective solution. That means that all those records and tapes that are currently in people's homes and Walkman machines and cars will still be copyable. The audio recording devices that made many of those tapes will be able to copy encoded or unencoded recordings for as long as they endure. When do you think the encoder could begin having a practical effect on the home taping problem?

Is it your position that despite this lag time the encoder technology will adequately protect the interests of creators?

RESPONSE

It will certainly be some time before the significant benefits of copy-coding are realized to any substantial degree. It is at this time impossible to predict the rate at which decoder-equipped recording devices will penetrate the market. That will depend on the development of taping technology, changes in production costs and consumer prices, and shifts in consumers' tastes.

While we cannot predict just when copy-coding technology "could begin having a practical effect on the home taping problem," we can predict with some certainty that it will be many years before such an effect is felt. For this reason, tape and equipment royalties are required as a short-term means of protecting the interests of copyright beneficiaries.

QUESTION

Wouldn't I be remiss if I didn't advise the good people of Maryland to start gearing up for the audio recording device repair industry?

RESPONSE

It is ironic that the same audio equipment manufacturers who take great pride in having successfully developed, produced and marketed several generations of recording equipment within a relatively short span of time are suddenly seized with doubts about their ability to find new devices which appeal to consumers. We have great faith that they will continue to develop recorders with new features and capabilities that will provide them continued commercial success.

If the equipment manufacturers are not successful in this regard, and if the people of Maryland choose to hold ontc their older machines and have them serviced and repaired, then there will emerge a Maryland-based job-producing repair industry, which would keep within the economy of Maryland revenues that would otherwise flow overseas.

Of course, how copy-coding affects the demand for repair services is an incidental issue. The primary consideration is that it would provide creators and producers of prerecorded music, including those of whom are your constitutents, with a measure of compensation for losses they sustain because of home taping.

QUESTION

The Congress has no desire to adversely affect those who make a living by selling audio recording devices. Why would anyone buy a new recording device that is less capable than one they already have? Would the sales of audio recording devices go down if the manufacturers included this decoder in their machines?

RESPONSE

We fully appreciate that Congress does not want to adversely affect the audio equipment industry. In avoiding such an impact, however, we hope that Congress will not ignore the adverse effect that home taping currently has on creators and producers of prerecorded music. In balancing these interests, Congress should take into account the needs of the America music community, which provides a unique product for our own consumption and for export to the rest of the world.

We have taken great pains to avoid any adverse impact on any of the relevant interests and to develop the copy-coding technology which -- like the tape and equipment royalties -- would not prohibit the copying of prerecorded music, but would merely provide a means for compensating copyright beneficiaries when their music is taped. The recording device equipped with a decoder would still be capable of copying pre-recorded music; the only difference would be that the machine would not be capable of doing so without providing a measure of compensation to copyright beneficiaries.

The only potential sales that might be lost if machines are equipped with decoders are those to individuals who are buying the equipment specifically so that they can tape copyrighted music without the authorization of copyright owners and without providing any compensation to copyright beneficiaries. If -- as the audio equipment manufacturers maintain -- few consumers are so motivated, few sales will be lost. In any event, *no* sales need be lost, because the equipment manufacturers can sell their machines *without* decoders by simply paying a royalty on such machines.

* * *

If I can provide you or any other Members of the Subcommittee with additional information, please do not hesitate to call on me.

Thank you very much for your continued interest.

Sincerely,

Stanley M. Gortikov

Stanley M. Gortikov

Senator **Mathias**. Thank you, Mr. Gortikov.

Mr. **Gortikov**. Thank you.

Senator **Mathias**. We have been joined by Senator Metzenbaum and Senator DeConcini. Let me call on them and see if they wish to make some opening statement. Then, we can proceed to questions.

OPENING STATEMENT OF HON. HOWARD M. METZENBAUM, A U.S. SENATOR FROM THE STATE OF OHIO

Senator **Metzenbaum**. Well, I continue to have some doubts as to whether requiring royalties on tapes and equipment is fair to consumers who would lean to more high-quality music.

But I am very interested in this new technology because I think that it zeroes in on the issue. I am sorry that I was not here to see the exhibition of it, but I am certain that your exhibit did work well and that it does provide some answers.

If it worked, that approach would mean that a consumer could decide whether he or she wanted to pay a little extra to have a tape or record that can be copied, as I understand it.

I think that it is a new factor in an old issue, and one that interests me very much. I want to be certain that it is fair and that whether or not it makes the market work better, how does it affect the consumers. I want to congratulate the industry on having come up with this solution. I do not know that it is a total solution, but it is certainly a major step in the right direction. I am very interested in how this hearing will go and what some of the opponents will say with respect to this particular subject.

Senator **Mathias**. Senator DeConcini.

OPENING STATEMENT OF HON. DENNIS DeCONCINI, A U.S. SENATOR FROM THE STATE OF ARIZONA

Senator **DeConcini**. Mr. Chairman, I have a statement I will ask to be submitted due to the time and my absence at the very beginning of the hearing.

Let me just say that I remain unconvinced that a fee on audio tapes and machines is necessary or appropriate.

I join the Senator from Ohio in my great interest in what was presented here today. I compliment the industry for coming forward with a proposed solution that does not just tax the consumer more for his or her quiet enjoyment.

And I ask that the balance of my statement be inserted in the record as if read. I do have questions at the appropriate time, Mr. Chairman.

Senator **Mathias**. Without objection, your statement will appear in the record.

[The prepared statement of Senator DeConcini follows:]

Prepared Statement of Senator Dennis DeConcini

Mr. Chairman, I will not have a lengthy opening statement this morning. We have had several hearings on the issues presented by S. 1739 over the last few years and my feelings about it are virtually unchanged. Briefly, I remain unconvinced that a fee on audio tapes and machines is necessary or appropriate. I do continue to be interested in finding ways to better reward creative artists, both writers and entertainers, for their efforts.

I understand that today's hearing will focus on two aspects of this issue which we have given only passing consideration previously. The first is the technology that would allow audio taping to be blocked by signals built into both the recording equipment and into the software itself. We will have a demonstration of this new technology this morning.

The second focus of this morning's hearing addresses a question that is of particular interest to me. This question is how the monies received through the fees proposed by this legislation will be distributed. I understand that the parties which would receive these fees have agreed on a distribution scheme which will be presented this morning. I am looking forward to reviewing these proposals.

Mr. Chairman, you have again assembled an impressive line-up of experts on this issue. I will carefully review the testimony and look forward to our discussion this morning.

Senator METZENBAUM. I am just curious about one thing.

Was it indicated, was this an ingenious American who developed this concept or an ingenious member of the Japanese community? [Laughter.]

Mr. GORTIKOV. I think Mr. McCoy takes credit for that at CBS.

Dr. McCOY. I will take credit for it on behalf of CBS Technology Center.

Senator METZENBAUM. And it was developed in this country?

Dr. McCOY. Yes, it was.

Senator METZENBAUM. Great. [Laughter.]

Senator MATHIAS. If it is agreeable to the committee, we will take questions in 5-minute segments.

Mr. Gortikov, is the record industry committed to offering encoded version of the music in all formats: Cassettes, albums, compact discs, and any other kind of medium that may be used for making sound recordings?

Mr. GORTIKOV. The industry is committed to offer a copy of both versions. Exactly what configurations will have to be developed by the marketplace and whatever is in demand at the time the technology takes root.

For example, the LP now is waning in its popularity as the compact disc comes on-stream. We will be responsive to consumer demand on configurations as those demands develop.

Senator MATHIAS. One thing that would concern the subcommittee is any negative effect on consumers who purchase machines equipped with the decoder.

It is your expectation that the industry would not offer exclusively, or even primarily, the uncopyable versions and thereby reduce or really destroy the value of the machines that are equipped with the decoder?

Mr. GORTIKOV. The expectation is that copiable versions would be available so that an individual who has a machine with a device in it is not unfulfilled in the ability to copy.

Senator MATHIAS. I think this is important because the Congress has to contemplate that if this encoding technology catches on, the record companies would find themselves in a very enviable position. You could either stop selling copyable albums and require customers to make more than one purchase. Or you could stop selling the uncopyable albums and require the customers to buy the more expensive product so that you would get an immediate return.

The market's adoption of this technology would really put you in a very strong position.

Mr. GORTIKOV. Well, the ultimate control also remains in the hands of the equipment makers because they would have an option either of putting out machines without the decoder chip on which they would pay a reasonable royalty—or putting out machines with the decoder chip.

Senator MATHIAS. Now, the position of the retailers is critical in this whole thing because copy-coding would require them to carry two inventories. That is important to you, to the public, as well as to the retailers themselves.

What sort of burden would that put on them?

Mr. GORTIKOV. Yes. But carrying dual or even multiple inventories is not strange to retailers in our industry. It began with 78's, with 10-inch and 12-inch records with LP's and 45's, cassettes and cartridges, and LP's and compact discs. So it was with mono and stereo. We have had multiple inventories throughout our history.

If you really want to see multiple inventories, however, go into a retail record shop, even of the witness coming onstream in a little while. Take a look at the blank tape inventory if you want to see multiple inventories. There you will really see replications of different brands of tapes that all do the same thing. The only thing they have in common is that they have no music on them. But, other than that, they are truly multiple, multiple inventories. So they are used to handling dual inventories.

Senator MATHIAS. Have any other products been crowded out by a multiple inventory? For example, you go into a supermarket and see New Coke, Diet Coke, and Classic Coke. Maybe Dr. Pepper got knocked out of some stores because of one of those formulations.

Do you know whether that kind of thing has ever happened?

Mr. GORTIKOV. Yes, sir, it certainly does.

If a given retailer does not expand his square footage, then he has to reduce the representation of product. That has certainly happened in our own industry as blank tapes become more popular and video—retail stores have been the outlet for video. Older catalog recordings have been diminished in the representation, for example, in most retail stores. So the store either expands or reduces total representation.

Senator MATHIAS. If he expands, that means that there is a greater capital demand.

Mr. GORTIKOV. Yes.

Senator MATHIAS. Now, let me ask you a tough question, because it is a hard one to answer. It is also an important question because the Judiciary Committee has antitrust jurisdiction as well as copyright jurisdiction.

If these encoders become accepted in the marketplace, can you estimate the amount of the premium that would be imposed on the copyable album?

Mr. GORTIKOV. No, I cannot. This would also be determined by the marketplace. So there is no way of my knowing what additional price, if any. Or a company could even choose not to put any added price on it if it wanted to.

We are fortunate in the assurance of having a highly competitive industry where the price factor has been very vigorously competitive in the past. I would expect that to be the same in the future.

Senator MATHIAS. But when you go into a record store, and you look at the records that are up on the various shelves and racks, they bunch together more or less in price categories, do they not?

Mr. Gortikov. Generally so. But if you look for advertisements in your Sunday paper, you will find bargains galore. The pricing practices of stores vary all over the lot. There are various price ranges in stores for different ages and popularities of recordings. New artists are often put out at lower prices. Older recordings are at low or mid prices. So there is true free-swinging price competition. And I would certainly expect that to continue.

Senator Mathias. My time is up, but I am going to pressure you for at least a guesstimate on this.

Senator Metzenbaum.

Senator Metzenbaum. Is this new technology ready to be implemented or is it still experimental?

Dr. McCoy. No. I think we are at the point where the design is complete. We have in preparation an integrated circuit chip that will accomplish the function which you have seen here today. The preparation of that chip will bring the cost down for the manufacturer to the range of $1 or under.

As I said in my testimony there, if they feel they have a better way to implement this, a different chip that will accomplish the same functions, this certainly would be permissible so long as they do not put in a chip that is easily to circumvent. In the chip we are designing, it would include certain critical functions of the recording circuitry and, therefore, its removal would also disable the recorder.

Senator Metzenbaum. How much would it increase the cost of the taping equipment?

Dr. McCoy. ~~Well, let~~ us see. If the parts cost is in the order of $1, there are standard markups, I think, from parts cost to retail costs in the order of $5 or $6 or so. So it might be in the order of $5.

Senator Metzenbaum. That is not on the tape, that is on the recorder.

Dr. McCoy. That is on the recorder, yes.

Senator Metzenbaum. On the recorder.

Dr. McCoy. There is no—it has no effect on the cost of the tape.

Senator Metzenbaum. No effect on the cost of the tape?

Dr. McCoy. No.

Senator Metzenbaum. As I understand what happens on the tape is that it plays and you can make a copy of it, but you would have some intermittent periods when it goes blank. Is that right?

Dr. McCoy. Yes.

Senator Metzenbaum. I am concerned about the problem of old equipment and using new tapes, new equipment using old tapes. I am also concerned about all the people who presently own equipment and cassettes.

What happens to them?

Dr. McCoy. OK. This is a case where anyone who presently owns a recorder will be able to continue to use that recorder and will be able to continue to copy tapes either that are protected by copycode or not. So for the older tape recording machine, there will be no reduction in their function.

Similarly, the new machines that are protected by the copy-code scanner will continue to be able to make copies of older recordings that are not protected with a copy-code signal. So the effect of this will take quite a long time to be felt as a significant portion of the new machines in use are protected by the copy-code scanner.

Senator METZENBAUM. So that if I had an old machine, and the new machines came out, and I just continued to use my old machine, I can continue making all the copies I want?

Dr. McCOY. So long as you can keep that old machine working, you could continue to make your copies.

Senator METZENBAUM. Mr. Gortikov, how does that then protect the industry since it is obvious that we are talking about 10, 15, 20 years until the equipment wears out, and besides, if it wears out, you can repair it if you want to make copies?

I am not sure how the new machine totally solves your problem?

Mr. GORTIKOV. Well, the proposal is, of course, that the royalty would prevail until the new generations of equipment ultimately take hold in meaningful quantities. So the royalty would cover that transition until that generation takes hold.

Senator METZENBAUM. How would you spell that out? I did not know that that was your proposal, because I came later. I guess maybe it is.

How long would that royalty continue in effect?

Mr. GORTIKOV. That would have to be determined. Also the provision in the proposed bill provides for the royalty tribunal to take into consideration changes in the marketplace.

So it could be sensitive to the dynamics of equipment population and trigger the time when the royalties might go down or be supplanted by the new technology.

Senator METZENBAUM. So that what you are now advocating is that Congress authorized the royalty and that then, at some future date, when there is lesser use of the old equipment, that whole procedure would phase out?

Mr. GORTIKOV. Correct.

Senator METZENBAUM. I have been around here a long time. Not that long, not as long as my chairman, but long enough to know that once somebody starts collecting money, whether it is the Federal Government or whomsoever else, they never stop. They never stop. I do not care whether it is the cigarette tax or telephone tax, they all come in saying they are going to phase out.

Would you agree to a time certain in the legislation with respect to the duration of the royalty, such as 3 years, 5 years? This way there would be something definite if we were to permit the royalty, a subject about which I still have some concern? But at least then we would know that it would only last for a definite number of years.

Mr. GORTIKOV. Yes, sir, I think that certainly is a feasible option to undertake. I agree with you on the continuity on the inclinations of perpetuating a benefit, as you just described. That is a problem we are meeting with the equipment and blank tape people. They continue to prosper at our expense. Our problem mounts constantly. Yet there is no diminution of their intent, no recognition of a problem, no willingness to talk to us about potential solutions.

As to the option that you are discussing, we would be more than happy to sit down and discuss that with our opposition. But I was part of an industry delegation to Tokyo to meet with the Japanese equipment and blank tape industry. We were absolutely stonewalled. There is no dialog possible so far, anyway. So we would welcome any options with specifics, such as what you just said, if we can get people to talk to us.

Senator METZENBAUM. Just one last question. It takes a yes or no answer.

If we were to require the use of this, whatever you call it, a copycode detector, on all new equipment, and there was no royalty, how would you feel about that, if that is the best you can get out of Congress?

Mr. GORTIKOV. Yes, that would be possible ultimately, but it would not solve any problems for a couple of decades until the generations of equipment took hold. So we are seeking that transitional royalty until that could take hold.

Senator METZENBAUM. Thank you.

Senator MATHIAS. Senator DeConcini.

Senator DECONCINI. Thank you, Mr. Chairman.

Gentlemen, this is intriguing and I think it is worthwhile pursuing. In order for the encoder technology to work, would not Congress have to mandate the manufacture of only encoded recording devices and encoded software?

Mr. GORTIKOV. No, sir. Because under the provision that we have, if an equipment manufacturer chose not to include a decoder chip and would, instead, prefer the payment of an equipment royalty, he would not have an obligation for the chip.

Senator DECONCINI. Well, if we did not do that, do you not think the marketplace will adjust so that only nonencoded recording devices and software are sold with the fee added which is required by this proposal?

Mr. GORTIKOV. No. The beauty of the proposal that we advance is is that it is a marketplace solution where the marketplace—the consumer has options, the manufacturer has options.

Senator DECONCINI. It seems to me that Congress would have to do some things for the recorder system to work. Correct me if I'm wrong about these.

First, mandate the manufacture of both encoded and nonencoded software.

Mr. GORTIKOV. Correct.

Senator DECONCINI. Two, have to mandate the sale of both encoded and nonencoded software.

Three, we would have to mandate that only encoded software could be played on the radio.

Mr. GORTIKOV. Correct.

Senator DECONCINI. Is that right?

Mr. GORTIKOV. Correct.

Senator DECONCINI. So we are really being asked——

Mr. GORTIKOV. Wait a minute. The first two options I thought were identical in what you described to me.

Senator DECONCINI. Mandate the manufacture of both encoded and nonencoded software

Mr. GORTIKOV. Yes.

Senator DECONCINI. Mandate the sale of both encoded and nonencoded software.

Mr. GORTIKOV. Well, I would think that the sale would be implicit in the manufacture too.

Senator DECONCINI. Yes.

So you would have to enforce that by law. It is intriguing to consider doing that.

But what does the consumer do? He walks into the retail store to buy a recorder, and the salesperson says for $50 more you can get one that you can record anything any place. He pays the $50 more.

Thereafter, he would then be able to buy the unencoded record or tape and be able to record it. He can buy the cheaper actual product because he had paid for the encoded one.

Mr. GORTIKOV. Correct.

Senator DECONCINI. Yes, the encoded one. And still be able to duplicate it if he wanted to.

Mr. GORTIKOV. But, based on the testimony just given, I would doubt that it would be $50. It sounds more like $5 or $6.

Senator DECONCINI. And I do not know what it would be. That was my question too. You said $5.

Would that be a $5 estimate on—regardless of the cost of the recorder because they vary from, I think, a few hundred dollars to a few thousand dollars?

Dr. MCCOY. No. Let me clarify the point I was making there. I thought I was being asked what would it add to the manufacturer's cost. What would he then have to charge in addition just to recover that cost of the additional chip?

Now, there would then be an additional charge that would amount to the royalty that would be above and beyond.

Senator DECONCINI. What do you think that would be?

Should Congress set that?

Mr. GORTIKOV. I missed the question. I am sorry.

Senator DECONCINI. What do you think that royalty would have to be, and should Congress establish what it is? Is $50 a unit or a percent or the purchase price, or what?

Mr. GORTIKOV. The royalty that is specified now for equipment is 5 percent of the wholesale price.

Senator DECONCINI. And you would want that——

Mr. GORTIKOV. And 25 percent for a dual cassette, that is, a multiple cassette recorder.

Senator DECONCINI. But you would suggest that we would add some percent on this new machine that has this chip?

Mr. GORTIKOV. Well, there would be no royalty on the machine with the chip. There would be no royalty on the machine with the chip.

Senator DECONCINI. Yes; I mean buy one without the chip. Excuse me. If you buy one without the chip.

Mr. GORTIKOV. The royalty on the ones without the chip.

Senator DECONCINI. Yes; and then what would the royalty be, the one that you bought without the chip?

Mr. GORTIKOV. The equipment without the chip would, in the language of the bill now, be 5 percent of the wholesale price or 25 percent in the case of a multiple-well recorder.

Senator DECONCINI. So you can buy either software if you buy the one without the chip?

Mr. GORTIKOV. Say that again.

Senator DECONCINI. You could buy either of the softwares—you would buy the cheapest product, record or tape—if you bought the one without the chip.

Mr. GORTIKOV. Yes.

Senator DECONCINI. OK.

Have you anticipated or dealt with the retailers of these recording devices of what their reaction is, and maybe we will hear that later, as to their having to carry perhaps six different versions of the same song and two different versions of the same recording machine? What kind of a burden does that put on them? Do you think that the market should adjust that?

Mr. GORTIKOV. I think just before you came in that question was addressed. And retailers have traditionally carried multiple inventories of recordings.

Senator DECONCINI. Have they carried as many as six different kinds?

Mr. GORTIKOV. I would say—I do not remember how many at one time. But at one time the cassette, cartridge, LP, single record, at least four of them; and mono and stereo, and now CD. There are more multiple inventories of blank tape than there are of prerecorded tape.

So multiple inventories are not new to the retailer. He, like we do, adjusts to consumer demand.

Senator DECONCINI. I see my time is up.

You do not think that that is posing an extraordinary burden on the software dealer to carry six different versions of the same song?

Mr. GORTIKOV. A problem, yes, that has to be reckoned with. But he regularly reckons with problems.

Senator Mathias, a few minutes ago, addressed the problem of Classic Coke and Diet Coke and regular Coke, all coexisting at the same time.

There is an interaction between the retailer and the consumer, and then between the retailer and the manufacturer. So this is a customary dynamic that we all live with all the time in our respective businesses.

The retailer has a protection which is unique to our industry. Recordings, sound recordings, whatever the configuration, are sold with a very, very liberal substantial return privilege. So the risk is on the manufacturer primarily, much more so than the retailer.

Senator DECONCINI. Thank you, Mr. Chairman.

Senator MATHIAS. I want to move on to the next panel just as quickly as possible, but I have got just a couple of questions.

Mr. McCoy, just so we are sure we understand what the technology here is: this is not a sublimial message that you add. It is something you take away.

Dr. MCCOY. That is correct. It takes away an almost infinitesimal slice of the sound energy above the normal range of the fundamental of the musical notes.

Senator MATHIAS. So there is not going to be some subconscious message telling me to run to the refrigerator or anything of that sort?

Dr. MCCOY. No, absolutely not. [Laughter.]

Senator MATHIAS. And I must confess, and I am sorry the others did not hear the demonstration, I could not tell any difference. My ear is not the best tuned ear.

Senator METZENBAUM. Let us do it over again. [Laughter.]

Senator MATHIAS. Let us arrange that for you later in the day if we can. We are up against that cloture vote and we have to get all these witnesses in.

I could not tell any difference. But there are a lot of people—and some of them in my family—who consider themselves real experts in this thing, and whose ears are more discriminating than mine.

What have you done to ensure, over and above what the scientists in your laboratories tell you, that no listener can really tell the difference between these two sets of signals?

Dr. McCOY. All right.

First of all, let me say that this is a situation where we have a fortunate ability in that the ear and brain complex together. It is quite used to the problem of supplying missing information on overtones of sound, something that we do every day of our life, every minute of our life. It is a very familiar situation where, if you are standing, let us say, close to some reflecting surface, you will have sound coming to you from two different paths, and if those two sound paths differ by an odd number of half wave lengths, you get a cancellation. And your ear is used to that situation and the mind supplies the missing sound energy at that point.

So that is something that works to our favor. We have done a considerable amount of informal testing at CBS, using our best ears to make sure that we cannot hear it and, in fact, we cannot. We have gone beyond that. We have supplied tapes, both coded and unencoded of the same material to RIAA engineers all over the country who have performed very demanding tests, A-B tests in which you compare synchronized encoded and unencoded recordings and switch instantaneously back and forth so that if there is any portion of that music that has been deteriorated, you will be able to detect it. And they have not been able to find a difference under those circumstances.

Mr. GORTIKOV. These are the engineers from individual recording companies, seven or eight of them.

Senator MATHIAS. Let me ask you very briefly.

What about obsolescence? People who have got eight-track systems a few years ago were told they were fixed for life. Now, suddenly, that configuration is obsolete.

I know no one can predict obsolescence, but what is your best guess? If people buy this equipment, are they going to find it useful for a long period of time?

Dr. McCOY. Yes; I do not see anything that would obsolete the equipment so long as the copy-code signal or technique that is used continues the same. Then it would continue to be protected by the scanners and the older equipment and the newer equipment. The same kind of protection can be extended to any new devices that come along.

Senator MATHIAS. I am going to give the rest of my questions to you in writing. You can respond in writing for the record and save time so we can move on to the next panel.

Let's go back to the one unfinished question I left Mr. Gortikov.

A 45-minute album today, let us say, sells for $7. We are talking about a 1-cent per minute royalty on blank tapes. So that is 45 cents to tape the 45-minute album. And then you add some little share of the royalty on recording devices.

So am I in the ball park to say that a copyable version would not sell for more than about $8 as against the $7 we are looking at today, or roughly 15 percent?

Mr. GORTIKOV. I am in no position to answer that.

There are antitrust concerns. There is no knowledge or experience directly in our industry to rely on.

The software industry, of course, does have copiable and uncopiable versions at different prices. I am not too familiar with how that varies.

Senator MATHIAS. We will leave my "guesstimate" on the record for the time being.

Mr. GORTIKOV. OK.

Senator MATHIAS. I am going to submit the rest of my questions to you in writing and request that you answer them for the record. Thank you.

Senator Metzenbaum.

Senator METZENBAUM. No more questions.

Senator MATHIAS. Thank you, gentlemen.

We will move on to our next panel, Mr. Jack Golodner, director of the Department for Professional Employees, AFL-CIO; Mr. Robert Summer, president, RCA Red Seal in New York; Mr. Ervin Drake, composer and past president of the Songwriters Guild of America.

Gentlemen, it is a pleasure to have you with us.

STATEMENT OF ERVIN DRAKE, COMPOSER AND PAST PRESIDENT, SONGWRITERS GUILD OF AMERICA, GREAT NECK, NY, ACCOMPANIED BY JACK GOLODNER, DIRECTOR, DEPARTMENT FOR PROFESSIONAL EMPLOYEES, AFL-CIO, WASHINGTON, DC; AND ROBERT SUMMER, PRESIDENT, RCA RED SEAL, NEW YORK, NY

Mr. DRAKE. Mr. Chairman and members of the subcommittee, my name is Ervin Drake. I am a composer and lyricist, as a matter of fact, of such songs "I Believe, For Every Drop of Rain That Falls, A Flower Grows," "When I was 17, It Was A Very Good Year," and I am the immediate past president of the Songwriters Guild of America. I am here today representing songwriters and music publishers.

I am joined by Robert Summer, president of RCA Red Seal, representing record companies, and Jack Golodner, executive director of the Department for Professional Employees, AFL-CIO, representing musicians, vocalists, and featured recording artists.

We appear before you to testify about the music community's proposal for disposition of the royalties generated by S. 1739.

There are three essential features of the distribution and selling arrangements that we propose. We propose, first, that a portion of the royalty be dedicated to a musical arts endowment for the benefit of aspiring songwriters and artists.

Second, we propose implementation of a distribution system in which 80 percent of the royalty pool would be shared by 100 percent of copyright beneficiaries, while the remaining 20 percent would be given as creative incentive grants to those whose work is not in substantial public demand.

Finally, we propose that S. 1739 be amended to prescribe a detailed formula for the sharing of royalties among copyright beneficiaries.

We will now address each of these components separately.

The music and arts endowment presents a means by which the musical community can help to promote the development of new music and assist those songwriters, musicians, and vocalists not yet lucky enough to have been published or recorded.

Specifically we propose that 1 percent of the royalty pool be contributed to the Songwriters Guild Foundation, which supports aspiring songwriters by giving them scholarship, workshops in which they hone their craft learning more about the craft of lyric writing for the top hundred and composition, even going as far as teaching them harmony and theory, those who do not have it. And we have had, in these various workshops, emerge such important people as Carol Hall, who tried out her score and was critiqued by the very workshop in which she was a student, to write the score for that very successful Broadway musical, "The Best Little Whorehouse in Texas." We have chart writers who owe the fact, not only to their own talents and energies, but to the work that they did under our foundation at the guild.

Another 1 percent should be allocated to the National Endowment for the Arts which would be instructed to commit these funds to a foundation to support aspiring vocalists and musicians. Through distributions made by both of these organizations, the music community would be able to provide seed money to nurture new talent and foster development of new types of music, important functions that have been undermined by the sale displacement caused by home taping.

The music community also proposes that the remaining royalties be distributed according to the following arrangements: 80 percent of the royalty pool would be shared by 100 percent of the copyright beneficiaries and distributed in direct proportion to the air play and sales of their musical recordings. Use of air play and sales data office and efficient means of identifying the music that is being played. Air play data also ensures that royalties will be allocated to more specialized music forms that reach a wide audience through broadcasts, as well as to older records that may be home taped but are no longer available for sale.

The remaining 20 percent of the royalty pool would be distributed by additional compensation in the form of greater incentive grants to those who received the smallest share. We presently envision that it would be about the lowest third of the home taping royalties. These grants would provide additional revenues to those most in need of a financial incentive to continue to produce their music, those struggling artists and song writers whose work has not yet been discovered by the public.

These grants would also encourage record companies and music publishers, particularly smaller labels that produce work in the narrow markets like jazz and classical music to support new music that is not yet commercially successful.

Finally, the music community proposes, on the basis of good faith negotiations among our industry constituencies, a royalty sharing formula that represents what we believe to be a fair and reasonable division of the royalties generated by S. 1739.

As you can see from the chart now being shown, we propose that royalties payable for each eligible musical recording be divided to give 2 percent to funds established by the AFM and AFTRA for the benefit of their performing artists; 23 percent to the songwriters and their music publishers to be shared equally by them; 30 percent to the featured artists on a recording; and 45 percent for the recording company, the copyright owner of the sound recording.

This allocation formula takes into account several possible approaches to the question of compensation for the various participants in the creative process. In arriving at it, the music community analyzed the amounts that different creators set when a record to which they contributed sold. The amounts that those creators lose when a sale is displaced by home taping and the very goals of S. 1739.

To illustrate how the proposed formula compares with the approximate distribution of royalties and income when records are sold, we have prepared the chart you now see to show the range of percentages that may be applicable to various types of records. As you can see, featured artists, union musicians, and songwriters will all receive more under our proposal than they would normally get when the record is sold. Our formula for royalty sharing thus helps to ensure that individual creators are adequately compensated for their labor.

These three proposals represent the fruits of a collaborative effort by the music community. We believe that they serve the policy goals of S. 1739 in a workable and fair way. All of us join in commending them to you and thanking you for their consideration.

[Mr. Drake's submissions for the record follow:]

PREPARED SUMMARY STATEMENT OF MR. ERVIN DRAKE

The music community has reached what it believes to be a workable and fair arrangement for the distribution of home taping royalties that furthers the policy goals of S. 1739. We propose the following:

That 2% of the royalty pool be allocated as a Musical Arts Endowment for the benefit of aspiring songwriters, musicians, and vocalists, that amount to be divided equally between The Songwriters Guild Foundation and the National Endowment for the Arts;

That the remaining royalties be distributed to the creators and copyright owners whose works were sold or broadcast during the relevant period as follows: 80% of the royalty pool would be shared by 100% of the copyright beneficiaries, distributed in direct proportion to the airplay and sales of their musical recordings; the other 20% of the royalty pool would be distributed as additional compensation, in the form of Creative Incentive Grants, to those who received the smallest share—about the lowest third—of the home taping royalties.

That the royalties payable for each musical recording be shared as follows: 2% to union funds for musicians and vocalists; 23% to songwriters and music publishers (the copyright owners of the musical composition), to be shared equally; 30% to the featured performing artist or artists; and 45% to the recording company (the copyright owner of the sound recording).

The benefits of this approach are manifold. First, it furthers fundamental copyright goals—the creation and dissemination of new music—by allocating a substantial portion of the royalty pool to the Musical Arts Endowment and Creative Incentive Grants, and thereby to those most in need of financial incentive to continue to produce their music. Second, it represents what we believe to be a fair and equitable arrangement for the sharing of royalties among all of those who are entitled to be compensated for the losses caused by home taping. Finally, it can be readily implemented, since the system would be administered almost entirely within the private sector, and distribution would be based largely on existing data.

For all of these reasons, the music community joins in recommending these proposals to Congress as an equitable implementation of the goals of S. 1739.

JOINT STATEMENT
OF
DEPARTMENT FOR PROFESSIONAL
EMPLOYEES, AFL-CIO
NATIONAL MUSIC PUBLISHERS' ASSOCIATION, INC.
RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC.
AND
THE SONGWRITERS GUILD OF AMERICA

INTRODUCTION AND SUMMARY

The Department for Professional Employees, AFL-CIO, the National Music Publishers' Association, the Recording Industry Association of America and The Songwriters Guild of America appreciate the opportunity to testify once again before this Subcommittee in support of S. 1739. As has been well documented in the past, home taping has caused a massive displacement of record sales, and has thereby undermined the music community's ability to continue to produce the diversified music that has been a hallmark of the American musical tradition. It is essential that a way be found to compensate creators and copyright owners ("copyright beneficiaries") for the losses they suffer when prerecorded music is copied rather than purchased.

Our testimony today focuses on both technological and economic mechanisms for compensation:

The technological mechanism, which we call "copy-coding," is a means by which inaudible signals encoded in recordings can be used to permit, or inhibit, home music taping. Under S. 1739, machines equipped with the "decoder" necessary to interpret the encoded signals are exempted from the payment of any royalty. Until now, the exemption has been largely conceptual.

Today we demonstrate that "copy-coding" technology is a reality.

Copy-coding offers a marketplace response to the home taping problem. The Japanese equipment manufacturers can choose: They can either exempt themselves from any equipment royalty by installing decoder chips in their machines, thus enabling American creators to protect their musical recordings, or they can pay an equipment royalty as compensation for the home music taping for which their products are sold. The choice is theirs.

The economic mechanism on which our testimony focuses today relates to the distribution of royalties collected pursuant to S. 1739. Specifically, we will present a model of a distribution system which furthers the public policy objectives of S. 1739:

- It allocates a portion of the royalties to a Musical Arts Endowment for the benefit of aspiring musicians, vocalists and songwriters.
- It establishes Creative Incentive Grants to assist those whose work is not yet in substantial public demand.
- It provides a formula for sharing of royalties among copyright beneficiaries.

We believe that the model is simple and cost effective, can use as its primary tool existing data that are readily available, and can be implemented on a voluntary basis with only limited government involvement. The model serves two fundamental copyright goals: it ensures that copyright beneficiaries will receive at least partial compensation for their home taping losses, and at the same time promotes the creation and dissemination of new music. We believe that it deserves the Subcommittee's full support.

I. THE COPY-CODING EXEMPTION: A MARKETPLACE ALTERNATIVE

The premise of S. 1739 is that those who profit from home taping should help those who are harmed by home taping. The manufacturers of blank audio tape and audio recording equipment design and market their products for the purpose of reproducing the copyrighted music we sell, displacing sales of our records. Those manufacturers should help offset the economic harm they cause; they should share some of the revenues they earn when they sell their home taping products with those in the music community who are hurt by those sales.

The legislation implements this revenue-sharing concept by requiring that royalties be paid on blank tape and equipment used for home music taping. To ensure that only those units likely to be used for that purpose bear royalties, the legislation contains several explicit exemptions.

Among the exemptions from the equipment royalty is one for machines ("audio recording devices") which contain

> a decoder or similar mechanism that prevents the device from reproducing, or permits the device to reproduce, the sounds embodied in a phonorecord or copy in accordance with special instructions encoded in the phonorecord or copy for that purpose.[1]

Until now, the decoder exemption has been largely conceptual. Today, we demonstrate that "copy-coding" is a reality -- that the technology which makes it possible is currently available, easy to implement, inexpensive and highly effective.

With this new technology, copyrighted records,

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[1] Because additional information about the specifics of such decoding mechanisms is now available, we suggest amending Section 2(d)(2) of the proposed legislation to provide greater definition to this decoder exemption.

tapes and compact discs can be encoded with an inaudible "notch" in the frequency spectrum. The notch can be detected by a special electronic scanning chip (a "copy-code scanner") installed in future generations of audio recorders. Recordings that are not encoded with the notch can be taped normally. Those which are encoded, however, cannot be taped; when the scanning chip in the machine detects the encoded notch, it periodically inhibits the recording function, leaving segments without sound on the taped copy.

Copy-coding means that the American music community need not be a helpless victim of taping technology. The same technical wizardry that has produced machines capable of appropriating our musical recordings can likewise be used to protect them. With the copy-code system, home tapers would still be able to reproduce our copyrighted music if they wish; they would simply be asked to pay for that privilege -- just as they already pay for multiple copies of anything else they buy.

Until now, the person who bought a prerecorded cassette for his own listening pleasure, never to be copied for anyone else, has had to pay the same price as the person who bought that same cassette with the intention of supplying copies of it to others. Not so with copy-coding. With this new technology, consumers can buy the type of recording they want: the purchaser who wants a recording just for use in his car would buy an "uncopiable" version -- one that is encoded with the notch. The person who intends to make multiple copies would buy a "copiable" version, which would have, included in its price, compensation for the copyright beneficiaries whose music is being taped.

Of course, copy-coding is strictly a prospective solution. Existing albums, tapes and CDs are not encoded and they will remain, as they are today, capable of being copied on any recording device, whether or not equipped with a decoder. Similarly, any recording equipment now in the marketplace or in any consumer's home will be, for the remainder of its useful life, fully capable of recording from both encoded and unencoded music sources. That is why we continue to need royalty legislation, because it would be decades before copy-coding can make a significant dent in the home taping problem.

But the technology does offer something very important right now -- a way for the marketplace to determine the most appropriate response to the home taping situation. The Japanese equipment manufacturers can decide whether they prefer the copy-coding approach or the royalty approach. Under S. 1739, machines equipped with a decoder chip are exempted from any royalty. The equipment makers are free to choose, therefore, whether to install decoder chips in their machines, or to pay a royalty instead.

If their devices are not being used to tape our copyrighted music, as the manufacturers claim, but are being used simply to enable people to record themselves playing the guitar or to tape class lectures or church sermons, then there can be no objection to the use of decoder technology. Decoder chips would not interfere with such uses, or affect any other non-infringing uses of audio tape recorders. They would do but one thing -- enable us to protect our copyrighted recordings.

The only reason manufacturers of recording equipment might choose not to install the decoder chips in their recording machines is so they can sell those machines for the purpose of reproducing our copyrighted music. They profit by selling machines which enable their customers to take our prerecorded music without paying for it. It is entirely appropriate that they pay an equipment royalty to those in the music community who are victimized by their practices.

In sum, the technology necessary to implement the "decoder" exemption in S. 1739 is now here, offering a fair, simple and efficient marketplace mechanism to respond to the problem of home taping.

A. How the Copy-Coding System Works

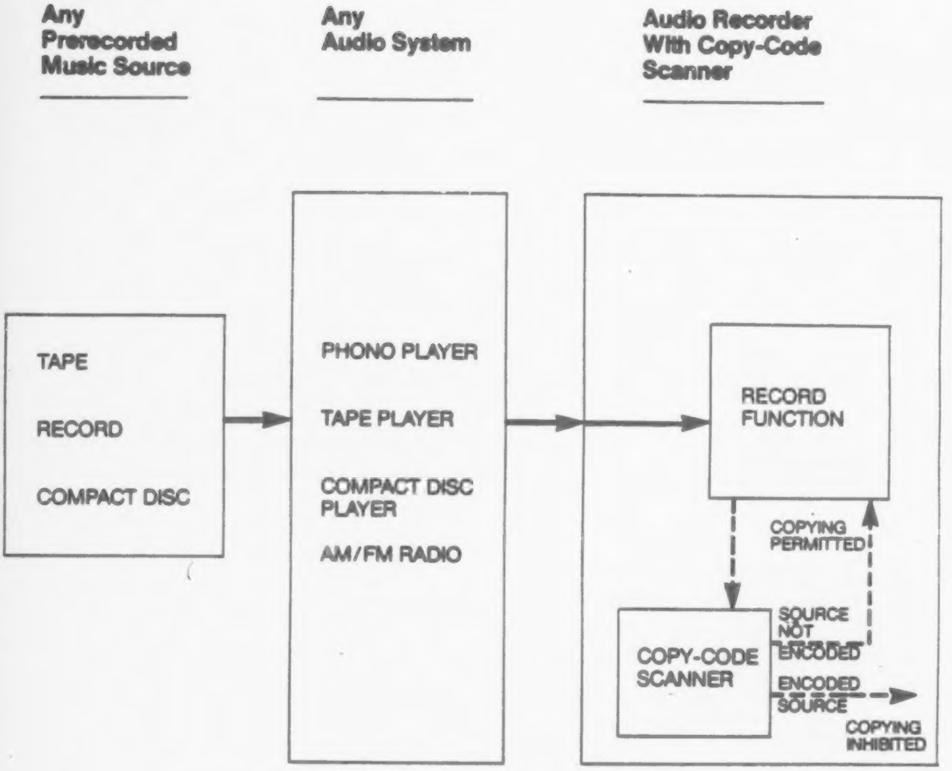
The copy-coding system, developed by audio engineering experts at the CBS Technology Center, has two elements: the encoder and the decoder.

-- The encoder is a small electronic device that can "encode" any master recording (whether in digital or analog form) by intermittently removing tiny slivers of sound high in the frequency spectrum (beyond the highest notes of any musical instrument and between the notes of the musical scale). To create this "notch" in the frequency spectrum, the recording is simply passed through the encoding device electronically. The notch thus embedded in the recording is effectively inaudible and does not affect the quality of the music.

-- The decoder is an integrated circuit ("IC") or chip designed to be built into the recording mechanism of future models of audio recorders. When the recording mechanism is switched on, the decoder scans the music, looking for the encoded notch, which is present only in uncopiable versions of copyrighted recordings. When the notch is detected, the decoder inhibits the recording function of the machine for a period of 25 seconds. The cycle is then repeated; if the scanner again determines that the notch is present, the recording function is interrupted for another 25 seconds. A copy taped from an "uncopiable" recording will thus consist of brief portions of music interrupted periodically by segments without sound.

The following diagram illustrates how the copy-code system allows normal copying of unencoded recordings, but inhibits the reproduction of recordings encoded with the notch.

COPY-CODE SYSTEM


Any Prerecorded Music Source
Any Audio System
Audio Recorder With Copy-Code Scanner
TAPE
RECORD
COMPACT DISC
PHONO PLAYER
TAPE PLAYER
COMPACT DISC PLAYER
AM/FM RADIO
RECORD FUNCTION
COPYING PERMITTED
SOURCE NOT ENCODED
COPY-CODE SCANNER
ENCODED SOURCE
COPYING INHIBITED

Copy-coding technology is presently available for implementation. Encoding devices have already been produced and successfully tested, and are ready to be manufactured in large quantities. A circuit board of the copy-code scanner has likewise been produced and tested, and a semiconductor chip version of the same circuitry will be available within a couple of months for mass production.[2]

The copy-coding solution is also cheap: the decoder chip is expected to cost less than $1 when mass quantities are produced. If manufacturers of audio recording devices are able to develop a compatible IC that can perform the same functions more efficiently or at lower cost, they would be free to do so. In any event, CBS has pledged to license both the encoder and the decoder that it has developed on a royalty-free basis for all hardware and software applications.

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[2] A technical description of the decoder's operation, a diagram illustrating the operation of the IC which will be installed in audio recorders, and the technical specifications of the system designed by the CBS Technology Center, are attached to this Statement as Appendix 1.

The principles of copy-coding can be adapted to all existing technologies and can be applied to all emerging formats as well. It is effective on every recording medium and method of electronic transmission. And it can be used on digital as well as analog recordings.

B. The Legislative Implications of Copy-Coding

Under the approach now embodied in S. 1739, recorders equipped with a copy-code scanner would not fall within the definition of an "audio recording device." This means that Japanese equipment manufacturers could choose for themselves whether to be exempted from any equipment royalty by deciding whether to include copy-code scanners in their machines. If they include the decoders in their machines, no royalties will be payable. Instead, by selling copiable recordings,[3] copyright beneficiaries will be able to collect some compensation directly from those who choose to tape our music, compensation included in the price charged for copiable versions of recordings.[4]

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[3] Making both copiable and uncopiable versions of recordings available will be no more burdensome to record companies, retailers or consumers than the introduction generally of new products or new configurations of existing products. The marketplace for recorded music is a perfect example of how an industry adapts to new technological and marketing developments -- from 78s to 45s and LPs, from mono to stereo, from phonograph albums to cassettes, and now to compact discs. Just as different configurations of the same prerecorded music coexist today, so new ones will coexist in the future.

If the Japanese equipment manufacturers choose not to utilize copy-coding technology, then it is fair to presume that they are selling their machines for the purpose of taping our music. In that case, it is reasonable to expect them to pay an equipment royalty to help offset the injury that such music taping will cause.

Use of copy-code technology to further the objectives of S. 1739 may require modifications in the legislation. In order to make copy-coding an effective alternative to the equipment royalty, the legislation should include a provision making it unlawful either to frustrate the operation of a copy-code scanner installed in a recording device or to provide another with the means with which to frustrate the scanner's operation. And to ensure that broadcasters do not inadvertently undermine the benefits of copy-coding, a provision should be added which requires broadcasters to play only encoded versions of recordings when such versions are available.

We want to emphasize that the implementation of copy-coding would in no way alter the fact that the audio home taping royalty will provide compensation for the copying of copyrighted musical recordings only. As we have previously indicated in written submissions to this Subcommittee, S. 1739 should be amended to specify that only audio recording devices are covered and that no royalty is to be imposed on videocassette recorders and other devices primarily used for reproducing motion pictures or other audiovisual works.

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[4] While this additional revenue will be distributed to copyright beneficiaries in a manner similar to that by which revenues from record sales are distributed, in light of the compulsory licensing provisions of Section 115, it would be necessary to specify in legislation the level of compensation that songwriters and publishers would receive from the sale of copiable recordings. The music community has already reached an understanding as to an appropriate formula for determining that level.

C. The Benefits of Copy-Coding

The copy-coding mechanism provides a practical and fair way to compensate music creators and copyright owners for some of the income they lose when people tape their music rather than buy it.

First, the copy-coding system offers a marketplace response to the home taping problem. When manufacturers elect to include copy-code scanners in their audio recording machines, no equipment royalty is imposed and government involvement is thereby minimized. Instead, the marketplace takes over. And in the best tradition of our economic society, the marketplace -- not the government -- will help determine the value of the right to copy recordings.

Second, the copy-coding approach is targeted: Those who wish to purchase new audio recorders only to tape their piano lessons or class lecture notes will simply purchase a royalty-free machine -- one equipped with a decoder. That way they will not have to pay an equipment royalty.

Third, the copy-coding system will not be impaired by future technological changes, nor will it impair them. This benefit is especially important now, with the advent of digital recording technology. A digital copy is of exactly the same sound quality as the source from which it is made. As digital recording becomes more common, the incentive for consumers to tape rather than purchase prerecorded music will increase: already the digital compact disc provides consumers with access to prerecorded music equivalent in sound quality to that of the originating master tape; the capability for digital-to-digital home recording has the potential to provide consumers with home recordings equivalent to the digital master recording itself. The copy-code system can be applied to these new technologies, not impeding their development and dissemination, yet ensuring that these new technologies do not impinge upon the rights of those who create and produce copyrighted music.

D. Legislation Is Required To Solve The Home Taping Problem

The Japanese equipment manufacturers have shown no willingness to help the American music community find a solution to the home taping problem. Indeed, they have rebuffed attempts by the American and international recording companies to meet with them, even in Tokyo, to discuss the problem. They prefer the status quo: they are selling millions of machines and hundreds of millions of blank tapes every year, products designed and promoted so that their customers can own the music we sell without paying for it.

Only Congress can provide the incentive for them to cooperate in solving the home taping problem. Only Congress can advance the vital public policy objectives of copyright -- ensuring that copyright beneficiaries, like other American workers, are paid for their labor, and assuring the continued production of the diversified music that has become a hallmark of the American tradition.

The copy-coding system offers a reasonable technological alternative. With that technology, the Japanese equipment manufacturers can exempt themselves from any equipment royalty. The choice is theirs.

But no matter how equitable the choices may be, they will not take any action at all, unless Congress acts. S. 1739, with its decoder exemption, is a responsible solution to the home taping problem. It should be enacted.

II. DISTRIBUTION OF THE ROYALTIES

Much of the discussion about S. 1739 has focused on how the proceeds from the proposed royalties on blank tape and recording equipment will be distributed.[8] To respond to the questions which have been raised, the music community, through negotiation and agreement among its constituencies, has developed a model for the sharing and distribution of the home taping royalties generated by S. 1739. In summary, we propose:

- Musical Arts Endowment -- that the first two percent of the royalties generated by S. 1739 be segregated to create a Musical Arts Endowment for the benefit of those aspiring songwriters, musicians and vocalists whose work has not yet been published or recorded;
- Creative Incentive Grants -- that 20 percent of the royalties available for distribution to copyright beneficiaries be given as additional compensation, in the form of Creative Incentive Grants, to those whose recorded work has not yet achieved widespread popularity; and
- Royalties to Copyright Beneficiaries -- that the royalties to which each musical recording is entitled be divided among copyright beneficiaries who participated in its creation based on a formula that blends prevailing industry practices and the policy objectives of S. 1739.

We discuss each of these proposals in greater detail below.

A. Disposition of the Royalty Pool

1. Musical Arts Endowment. To help promote the development of new music and to enhance the opportunities of aspiring songwriters and recording

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[8] S. 1739 provides that all copyright owners who have filed claims for a portion of the royalty pool -- those whose musical works or sound recordings were played on the radio, broadcast on television, or sold in the form of a phonorecord during the year for which the royalties are collected -- must negotiate in good faith among themselves in an effort to reach a voluntary agreement on the distribution of the royalties. The Copyright Royalty Tribunal is authorized to approve such voluntary agreements, but is required to conduct an evidentiary proceeding to determine the apportionment of the royalties in the event that a voluntary agreement is not reached.

artists, we believe that two percent of the total royalties generated by S. 1739 should be allocated to an endowment for the benefit of those musicians, vocalists and songwriters whose work has not yet been recorded. That endowment would be divided equally between (1) The Songwriters Guild Foundation, which would use the funds to aid new lyricists and composers,[6] and (2) the National Endowment for the Arts, which would be instructed to commit its share to a foundation to support aspiring vocalists and musicians.

These contributions would encourage and nurture new talent that might otherwise, for lack of financial support, remain undiscovered. They would also facilitate the development of new and experimental types of music which cannot be expected to gain immediate market acceptance. The Musical Arts Endowment would thus promote fundamental copyright goals: the creation and dissemination of new music.

2. Creative Incentive Grants. The music community believes that a portion of the total royalty pool should be targeted at those copyright beneficiaries who are most in need of additional incentive and whose works are not yet in substantial public demand.

We thus propose that 100 percent of the eligible copyright beneficiaries share 80 percent of the royalty pool, distributed in direct proportion to the airplay and sales of their musical recordings. The remaining 20 percent of the royalty pool would be allocated as "Creative Incentive Grants," additional payments to be distributed among copyright beneficiaries of those musical recordings that received the smallest share --

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[6] The Songwriters Guild Foundation offers aspiring songwriters scholarships to colleges, universities and schools of music, provides free studio time for unpublished songwriters, sponsors seminars and forums, and provides information services on all aspects of the music industry.

about the lowest third -- of the home taping royalties distributed to all copyright beneficiaries.[7]

This approach would target additional royalties to those lesser known or less successful lyricists, composers, musicians and vocalists who need a financial incentive to continue to produce their music. This approach would also encourage record companies and music publishers -- especially those small labels and companies that produce works aimed at narrower markets -- to take chances on such unknowns, since compensation from the royalty pool, enhanced by such grants, would offset some of the losses incurred when a work is not commercially successful. Along with the contribution made to the Musical Arts Endowment, therefore, this portion of the proposed distribution system would further a basic purpose of copyright law -- to encourage the creation and dissemination of new artistic work.

3. Royalty Sharing Formula for Copyright Beneficiaries. We propose that copyright owners and those musicians, vocalists, lyricists and composers whose works have been published and recorded share home taping royalties in accordance with a prescribed formula. The sharing formula would apply to 100 percent of the royalties designated for copyright beneficiaries (after deduction of the funds for the Musical Arts Endowment and any administrative expenses). Thus, it would apply to the portion of the royalty pool distributed in direct proportion to the airplay and sales of all musical recordings (80 percent of the pool), as well as to the portion distributed as additional compensation in the form of Creative Incentive Grants (20 percent of the pool).

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[7] The methodology for distributing royalties on a proportional basis and for allocating Creative Incentive Grants is described in Section II(B) and explained in detail in Appendix 2.

Under our proposed system, royalties payable for each musical recording (which includes both the sound recording and the musical composition embodied in it) sold or broadcast during the relevant period would be divided in the following manner:

- Two percent would be allocated to funds for musicians and vocalists (now in existence or to be established by the American Federation of Musicians (AFM) and the American Federation of Television and Radio Artists (AFTRA)). Of that two percent, 1-3/4 percent would be contributed to the AFM funds and 1/4 percent would be allocated to the AFTRA fund.
- 23 percent would be allocated to the songwriter(s) and to the copyright owner(s) of the musical composition (i.e., their music publisher(s)), to be shared equally.
- 30 percent would be allocated to the featured recording artist(s) normally compensated by royalty payments.
- 45 percent would be allocated to the copyright owner of the sound recording, i.e., the recording company.

This royalty sharing formula is intended both to mirror the sharing of royalties and income that copyright beneficiaries would have received had a sale of their work not been displaced by home taping, and to help serve the public policy objectives of the legislation. As part of the negotiation process, the music constituencies considered numerous factors and developed and analyzed a variety of approaches in order to determine appropriate sharing arrangements.

For example, the extent to which manufacturing, production, distribution and other costs and expenses may not be incurred when a sale is displaced by home taping was taken into account. Also, the relative revenue shares enjoyed by the various music constituencies when a record is actually sold were considered. Finally, considerable weight was given to the beneficial purposes to be served by this legislation -- not only to ensure that compensation is provided to those whose works have been taken without authorization, but also to foster and nurture the creation and dissemination of new musical works.

The product of all these deliberations is reflected in the community-wide agreement arrived at after good faith arm's-length negotiations. The music community is satisfied that the proposed arrangement is fair and reasonable for all the participants and that it amply serves the beneficial purposes of S. 1739. We join in recommending it to the Congress.

For purposes of illustrating how the proposed sharing formula compares with the approximate distribution of royalties and income when records are sold, we have prepared a chart depicting the range of percentages that may be applicable to the sale of various types of records:

Component Cost	Percentage of Wholesale Price	Percentage To Be Allocated Under Home Taping Royalty
Artists' royalties	15% - 24%	30%
Musical composition royalties*	10% - 15%	23%
AFM and AFTRA	1%	2%
Record Company (includes costs for marketing, artwork, manufacturing, distribution, advertising and overhead and profit)	60% - 74%	45%

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*Based on statutory rates.

As illustrated by these figures, while an average artist would ordinarily receive anywhere from 15 to 24 percent (and, in rare instances, more) of the wholesale price of a record, the music community proposes that each artist be given 30 percent of the home taping royalty to which his or her sound recording is entitled. Similarly, where union musicians and vocalists normally benefit from a contribution to the union funds of about one percent of the wholesale price of records on which they participate, we propose that they be allocated two percent of the royalties generated by the musical recordings they have helped to create. Songwriters and their publishers would also benefit by sharing 23 percent of the royalty pool, an amount in excess of their combined return when a record is sold.

Regardless of the sharing arrangements applied to the royalty pool, one fact should never be overlooked: that the royalties generated by S. 1739 will not even come close to making copyright beneficiaries whole for the losses they incur as a result of home taping.

B. Administering the Royalty Distribution System

To implement the goals discussed above, the system for distribution of royalties to copyright beneficiaries relies upon a two-pronged approach: allocating 20 percent of the royalties generated by S. 1739 and distributed to copyright beneficiaries for Creative Incentive Grants to benefit those whose work is not yet in widespread public demand; and allocating the other 80 percent of that royalty pool for distribution to 100 percent of copyright beneficiaries in proportion to airplay and record sales data.

Use of airplay and record sales data as the basic tool for division of the royalty pool would provide several benefits. First, airplay and record sales data are primary indices of which albums and tunes are most in public demand, and thus are an effective and simply implemented proxy for identifying the musical recordings that are being taped. Use of these data would therefore permit the bulk of the royalties to be distributed in accord with the fundamental principle that those who are injured as a result of home taping -- the copyright owners and creators of a taped tune -- are the ones who should be compensated by a royalty. Use of airplay data also ensures allocation of royalties to more specialized musical forms (e.g., classical music and jazz) that reach a wider audience by broadcasts than by record sales, as well as to those older tunes and phonorecords that may be home taped but that are no longer available for sale.

The distribution system would thus require the collection and appropriate weighting of airplay and phonorecord sales data; the determination of the share to which each musical recording is entitled; and the disbursement of royalties to eligible copyright owners following approval by the Copyright Royalty Tribunal of an agreed upon allocation. We believe that having a private sector administrative organization implement all of the steps in the distribution system would be the best approach. This supervisory function could even be performed by an existing organization to avoid any additional costs that might be incurred by a new entity created specifically for this purpose.

A step-by-step analysis of proposed distribution procedures is set forth in Appendix 2.

* * *

This royalty allocation proposal represents the fruits of a collaborative effort by the music community. The mechanics of the approach are simple and equitable, employ existing data that could be readily adapted for this purpose, and could be administered with minimal government involvement. Moreover, such an approach is most likely to avoid lengthy and costly evidentiary proceedings before the Copyright Royalty Tribunal, and would permit the bulk of the royalty pool to be used, as it was intended, to compensate creators and to ensure the continued production of the diversified music that has become an American tradition.

APPENDIX 1

CBS COPY-CODE SYSTEM

CBS
TECHNOLOGY
CENTER
CBS Inc. 227 High Ridge Road
Stamford, Connecticut 06905
(203) 327-2000

TECHNICAL DESCRIPTION OF THE CBS COPY-CODE SYSTEM

1. Copy-Code Encoder

The encoder processes each channel of a stereo signal separately. The narrow bandstop filter that the encoder inserts in the signals has a center frequency of 3840 Hz. The 3 dB attenuation frequencies are plus or minus 125 Hz and the ultimate attenuation of the center frequency can be adjusted between -12 and -80 dB. The filter is constructed from active operational amplifiers and is a sixth order Chebyshev design using three biquad filter stages connected in series. The bandpass filter output from each biquad filter stage is subtracted from a direct signal path so as to create a bandstop filter. The biquad filter is both versatile and stable and the residual frequency response ripple in the pass band is very small (less than ±0.01 dB).

The coder has a bypass position activated by a switch. This permits input signals to be passed directly to the output without encoding. The encoding equipment employs normal professional quality audio circuit techniques.

A purely digital-to-digital encoder has also been developed using a computer derived notch filter with the same technical specifications as the analog unit. The filter is a sixth order Chebyshev type 2 design. When the hardware for this is complete, encoding of digital programs will occur during digital mixing or editing, before the master program tape is made. Encoded master tapes would be sent out to the manufacturing facilities and would be used to make records, cassettes, CD's and other software products.

2. Copy-Code Decoder

The purpose of the decoder is to detect the presence of the copy-code in audio signals. It can be used in any type of audio recording machines, disabling the recording process wherever a copy-code is found. The decoder functions by comparing the audio energy present at the frequency of the notch, with the energy immediately adjacent to the notch and on either side of it. If the decoder finds equal amounts of energy, then the program was not encoded and no action is taken. If on the other hand, it detects significantly less energy at the notch frequency, then, after a process of careful electronic tests to ensure that the conclusion was correct, action is taken to stop the recording.

The circuit operates as follows:

The left and right channels of the input audio signal are summed together, only for the purpose of providing a side-chain monophonic input to the detector. The signal is then applied to a third-order bandpass filter whose response is centered at the notch frequency, 3840 Hz, and whose -3dB bandwidth is 750 Hz. This bandwidth is about three times the bandwidth of the bandstop, or notch, filter in the encoder. The signal is then passed through a fast-action automatic gain control system. This circuit sets the average level of the output signal to a constant value, i.e., it raises the level of "quiet" input signals and reduces the level of "loud" signals to ensure that, irrespective of the nature of the program material being presented to the detector, the same average signal level is maintained.

The constant level signal is now divided between two paths. One path feeds a narrow bandpass filter, of the same bandwidth and center frequency as the bandstop filter in the encoder. This is followed by a full-wave rectifier and first integrator whose integration time constant can have one of two different values, selected by a control circuit. The other path feeds a second full wave rectifier and integrator with two alternate time-constants identical to the first. Both integrators have time-constants which are switchable between 80ms and 13 seconds.

If the music is not encoded, then the D.C. outputs from the first and second integrators will be the same. If, however, encoded music is used, then the D.C. output of the first integrator will remain at a small value, while the output of the second integrator will be much greater. A comparator, which detects the ratio of these values within a preset margin of tolerance, thus determines the presence of the "notch" in the music signal. This will only occur if the program was copy-coded.

The two integration time constants help ensure the decoder's faultless performance. Initially, the short time constant of 80ms is set by the control logic in the detector, and a special generator sweeps the center frequency of both the 750 Hz and notch bandpass filters in synchronism by +6%. This function is known as the "search" mode, and is engineered to look for the notch in the event that the software to be copied is being played up to 6% too fast or slow. (For example, the signal source could be a record player whose turntable speed is 34 r.p.m. instead of 33 1/3 r.p.m.). If the detector comparator produces an output which indicates that a notch has been detected, the control logic stops the frequency-sweep and simultaneously switches both integrators to the 13 second time constant, and no other action is taken at this time. After 13 seconds, the output of the comparator is again diagnosed. There are two possible conditions:

(a) A notch has been found. Action is then taken to disable the recording for 25 seconds. After this period all the circuits are reset and the whole cycle starts again.

(b) No notch is discovered, and the original trial indication was a false alarm. Action is taken to reset the logic and the whole cycle is repeated until another possible notch frequency location is found. Meanwhile, the recording continues uninterrupted.

If there is any doubt that the music was encoded, the circuit allows the recording to continue. The decision to disable the recording is only made when a definite notch is discovered continuously for 13 seconds using the double time-response technique.

Finally, there are logic and control circuits built into the detector. These regulate the timing cycles, the frequency sweep, integrators and other necessary functions. The control circuit also has outputs that are used to switch the recording process off if a successful detection of encoded material has been made. Moreover, the center frequency of the filters will track correctly in the case of twin transport cassette decks that copy tapes at twice or four times normal speed. In these cases, the center frequency of the notch will be at 7,680 and 15,360 Hz respectively. The detector circuit will automatically change to search for a notch ±6% about these frequencies.

An 18 pin integrated circuit is being developed to perform all of the above functions. When manufactured in bulk quantities it will cost equipment manufacturers about $1.00.

CBS
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COPY-ENCODER MODEL 8300

TECHNICAL SPECIFICATIONS

Inputs:	Active differential balanced
Input Impedance:	10K ohms balanced input 5K ohms unbalanced (single ended input)
Input Level:	+20 dBm maximum (Ref. internally generated OdBm reference)
Outputs:	Floating, active balanced
Output Impedance:	100 ohms
Output Level:	+24 dBm, just before clipping into 600 ohm load
Frequency Response:	
Bypass Mode:	+0, -0.1 dB 20 Hz - 20 kHz Bypass Mode
Encode Mode:	Same as Bypass mode except with the inclusion of a band reject (notch) filter centered at 3840 Hz. Maximum notch depth -60 dB at center. 3 dB points 3688 Hz and 3965 Hz, ±3%.
Distortion:	Less than .02% THD 20 Hz - 20 kHz to +24 dBm
Signal/Noise (Bypass):	Greater than 90 dB
(Encode):	Greater than 90 dB (Referred to a OdB input, over a measurement band of 30 kHz)
Power Requirements:	115VAC or 230VAC (selectable via line voltage programming card) 50/60 Hz, 30VA.

CBS COPY-CODE SYSTEM

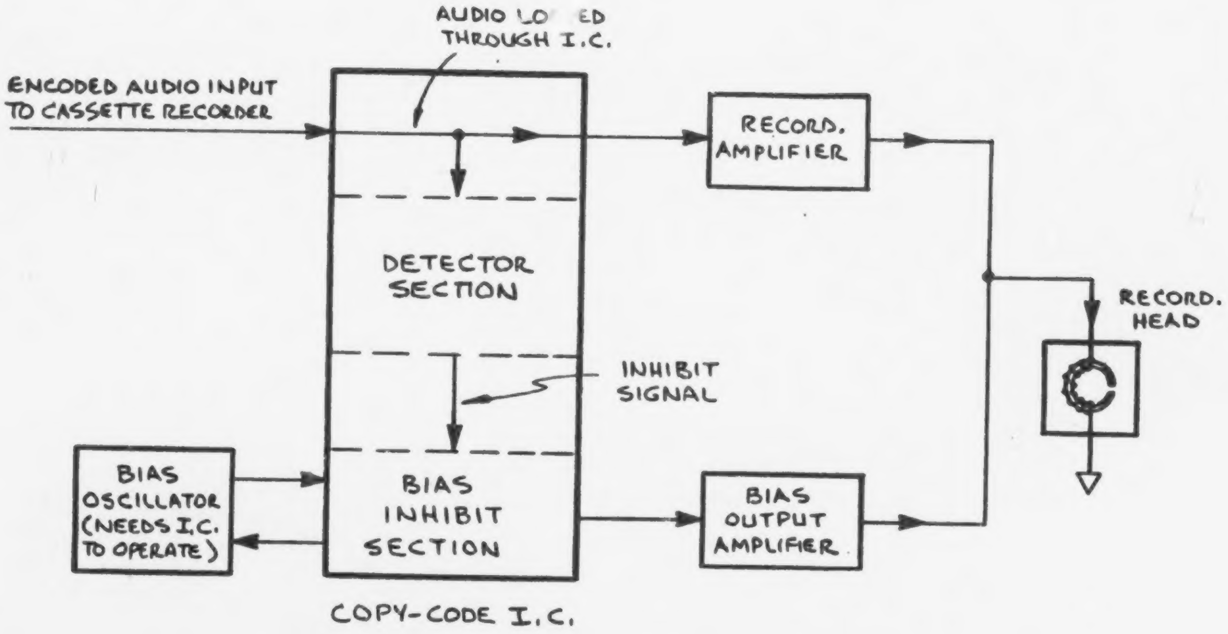

AUDIO LOOPED THROUGH I.C.
ENCODED AUDIO INPUT TO CASSETTE RECORDER
RECORD. AMPLIFIER
DETECTOR SECTION
RECORD. HEAD
INHIBIT SIGNAL
BIAS OSCILLATOR (NEEDS I.C. TO OPERATE)
BIAS INHIBIT SECTION
BIAS OUTPUT AMPLIFIER
COPY-CODE I.C.

DIAGRAM ILLUSTRATING OPERATION OF COPY-CODE INTEGRATED CIRCUIT (I.C.)

APPENDIX 2

ADMINISTRATION OF THE ROYALTY DISTRIBUTION SYSTEM

The following is a step-by-step analysis of the procedures necessary for implementation of the distribution system proposed by the music community.

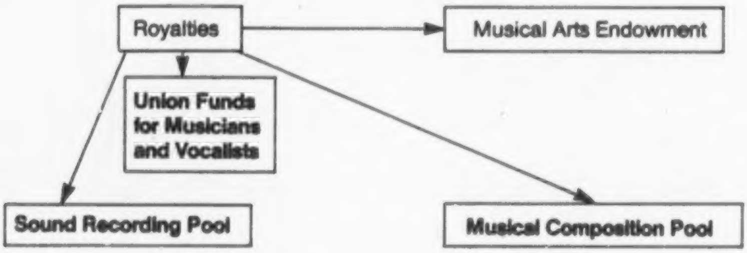
1. Collection of the Royalties. Collection of the royalties under S. 1739 of course must precede their distribution. The bill provides that manufacturers and importers of blank audio tapes and taping equipment will pay a one-time royalty per unit when they first sell or distribute their products in the United States. The proceeds of that royalty are to be collected by the Register of Copyrights and ultimately transferred to the Copyright Royalty Tribunal for distribution. Allocations under the distribution system described below would be submitted for Tribunal review and approval as the result of a collaborative effort by the music community.

2. Contribution to the Musical Arts Endowment

Royalties
Musical Arts Endowment

The first step in the distribution process would be to allocate two percent of the entire royalty pool to the Musical Arts Endowment. That endowment would be divided equally between The Songwriters Guild Foundation and the National Endowment for the Arts for the benefit of aspiring lyricists, composers, musicians and vocalists.

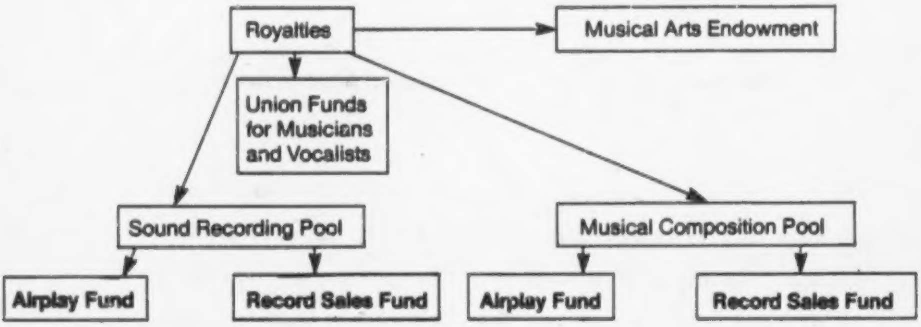
3. Division of the Royalties into Copyright Pools


Royalties
Musical Arts Endowment
Union Funds for Musicians and Vocalists
Sound Recording Pool
Musical Composition Pool

The second step in the distribution process would be to divide the remaining royalties in the royalty pool among the two copyrights encompassed in every musical recording -- the musical composition and the sound recording -- and the union organizations representing musicians and vocalists.[1] The Musical Composition Pool would consist of the shares of the royalties to which lyricists, composers and publishers are entitled; the Sound Recording Pool would consist of the shares of the royalties to which artists and record companies are entitled.

Each of these pools would be further subdivided as described below.

4. Division of the Copyright Pools Based on Record Sales and Airplay Data


Royalties
Musical Arts Endowment
Union Funds for Musicians and Vocalists
Sound Recording Pool
Musical Composition Pool
Airplay Fund
Record Sales Fund
Airplay Fund
Record Sales Fund

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[1] The two-percent contribution to union funds would be distributed separately based upon the union's own data.

Numerous surveys have established that music is taped from two primary sources: from radio and television broadcasts, and from phonorecords. In order to fairly compensate copyright beneficiaries for the losses they suffer as a result of home taping from both media, it would be necessary to divide the copyright pools into separate funds that mirrored the relative amount of taping attributable to each of these primary sources of home taping. Home taping royalties could then be allocated based on data that reflected both the amount of airplay a musical recording had received and the sales that that recording had enjoyed.

The music community thus proposes that a survey be conducted annually to establish the proportion of taping that is attributable to airplay and the proportion that is attributable to record and tape sales.[2] The Musical Composition Pool and the Sound Recording Pool would then each be subdivided, in the percentages dictated by the survey, into two funds: the Airplay Fund and the Record Sales Fund.

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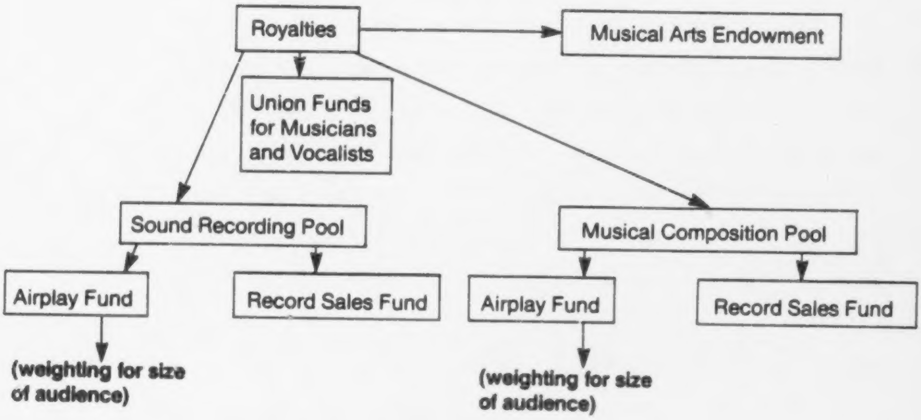
[2] Audits & Surveys, in its comprehensive survey of home taping conducted in 1983, found that 31 percent of the volume of music taped annually is taped from the radio, and that 60 percent of home taping is done from records or prerecorded tapes. Audits & Surveys also determined that 7 percent of taping is done at concerts, while 2 percent of taping is done from home tapes of music. The music community proposes that taping from concerts be treated for distribution purposes as if it were taping from the radio, and that the percentage of taping that is done from home tapes -- taping whose original source is unknown -- be allocated in the same proportion as the copyright pools are divided into airplay and record sales funds.

5. Allocation of the Airplay Funds: Monitoring and Weighting of Airplay Data


Royalties
Musical Arts Endowment
Union Funds for Musicians and Vocalists
Sound Recording Pool
Musical Composition Pool
Airplay Fund
Record Sales Fund
Airplay Fund
Record Sales Fund
(weighting for size of audience)
(weighting for size of audience)

The Airplay Funds in both the Sound Recording Pool and the Musical Composition Pool would next be weighted to reflect the size of the audience. Compilation of the data necessary to achieve this weighting could be performed by either of two existing performing rights societies -- ASCAP or BMI. These two societies have for years distributed royalties to composers, authors and publishers for public performances of musical works over radio and television and before live audiences. Each organization uses statistically valid sampling techniques to monitor all music broadcast. Each then assigns weights to the assembled data in accordance with formulae that take into account the time and place of performance, so that royalties can be fairly allocated based on the size of the audience that is likely to have listened to the copyrighted tune.

These data bases could be readily used to assist in distribution of home taping royalties on the basis of airplay.[3] Because both ASCAP and BMI maintain competing and overlapping data bases, the private organization that administers the distribution system could bargain with each collecting society to obtain the most economical rate for use of its data base. Such an arrangement would also be attractive to the collecting societies, as it would enable them to share the costs of data collection and compilation and thereby reduce their own expenses.

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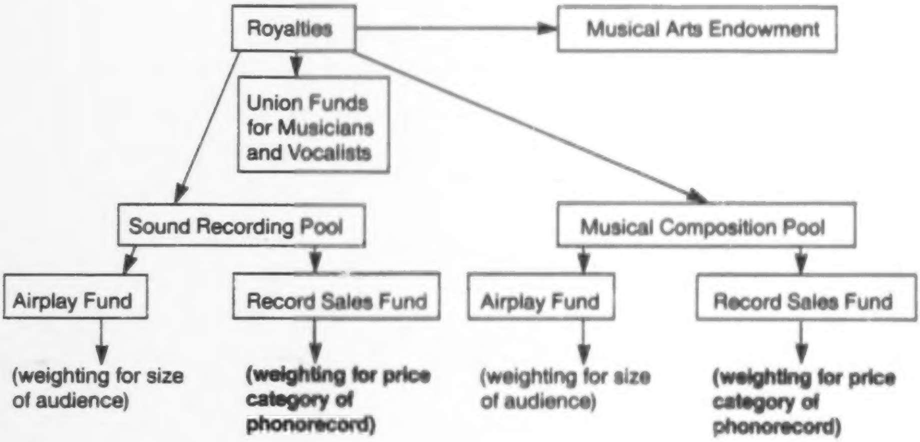
[3] Although the data bases do not currently include information on the artist and particular recording featured during a radio or television broadcast, such additional information could be efficiently obtained.

6. Allocation of the Record Sales Funds: Monitoring and Weighting of Record Sales Data

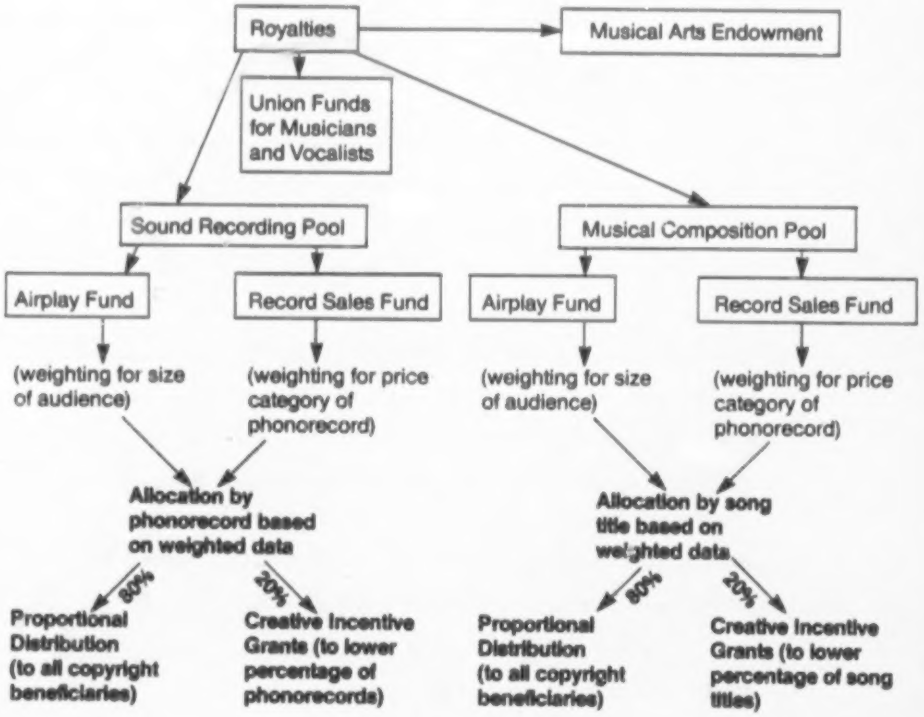

Royalties
Musical Arts Endowment
Union Funds for Musicians and Vocalists
Sound Recording Pool
Musical Composition Pool
Airplay Fund
Record Sales Fund
Airplay Fund
Record Sales Fund
(weighting for size of audience)
(weighting for price category of phonorecord)
(weighting for size of audience)
(weighting for price category of phonorecord)

Record companies maintain data on sales of phonorecords that could be readily adapted for the purposes of this legislation. Under the proposed distribution system, record companies would submit these data in confidence to the system's administering organization (or to its agent) for use in allocating the Record Sales Funds in both the Sound Recording Pool and the Musical Composition Pool. To compile a data base for allocations by tune in the Record Sales Fund within the Musical Composition Pool, a master listing setting forth each tune's title and publisher need be submitted only once for each phonorecord.

Data submitted for allocation of the Record Sales Funds in both Copyright Pools would also be assigned an appropriate weighting factor to reflect the different economic impact that home taping has when it displaces the sale of a front-line album as compared with, for example, the sale of a budget-priced album. To account for this differential in loss, the proposed distribution system would divide records (and their component tunes) into appropriate price categories, e.g., budget, mid-price and front-line, based on the different prices charged for different records. Such price information would be readily available from present and past record company catalogs.

7. Calculation of Royalty Allocation

Based on the collection and weighting of the data described above, each musical recording would be entitled to one or both of two components of the royalty pool: first, a proportional distribution of royalties based on relative airplay and sales; and second, a Creative Incentive Grant.


Royalties
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Musical Composition Pool
Airplay Fund
Record Sales Fund
Airplay Fund
Record Sales Fund
(weighting for size of audience)
(weighting for price category of phonorecord)
(weighting for size of audience)
(weighting for price category of phonorecord)
Allocation by phonorecord based on weighted data
Allocation by song title based on weighted data
80%
20%
80%
20%
Proportional Distribution (to all copyright beneficiaries)
Creative Incentive Grants (to lower percentage of phonorecords)
Proportional Distribution (to all copyright beneficiaries)
Creative Incentive Grants (to lower percentage of song titles)

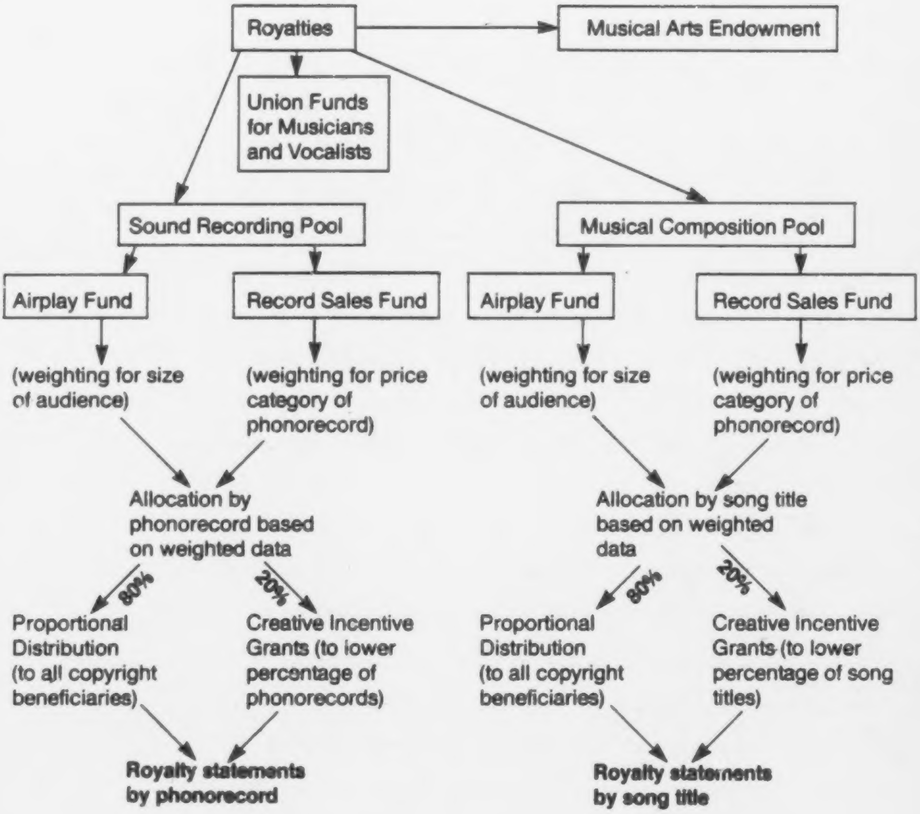
a. Proportional Distributions. The music community proposes that 80 percent of the royalties available for distribution to copyright beneficiaries be distributed to 100 percent of eligible copyright beneficiaries in direct proportion to the airplay and sales of their copyrighted works. Mechanically, what this means is that 80 percent of the Airplay and Record Sales Funds of both the Sound Recording Pool and the Musical Composition Pool would be allocated to 100 percent of all eligible copyright beneficiaries in proportion to weighted airplay and record sales data, respectively.

b. Creative Incentive Grants

The remaining 20 percent of the royalties available to be distributed to copyright beneficiaries would be allocated for Creative Incentive Grants to be paid to those most in need of additional incentive. Based on the total payments previously made on a proportional basis from the royalty pools for each musical recording, those that received the lowest percentage of the payments would be entitled to receive an additional payment in the form of a Creative Incentive Grant. We presently envision that grants would be made to those that received the lowest third of the Proportional Distributions.

The purposes of these grants are severalfold. First, they would provide a financial incentive to those whose creative work is not yet in substantial public demand. Second, the system would be designed so that no copyright beneficiary awarded a Creative Incentive Grant would thereby receive more from the royalty pool than a copyright beneficiary compensated by Proportional Distributions alone. Finally, in accordance with fundamental copyright principles -- that payment should be made as compensation for loss -- the system would also be designed so that participating copyright beneficiaries whose work enjoyed greater sales or radio exposure would receive a greater royalty than those whose work was less exposed, albeit at a smaller marginal rate.

8. Distribution of the Royalty Pool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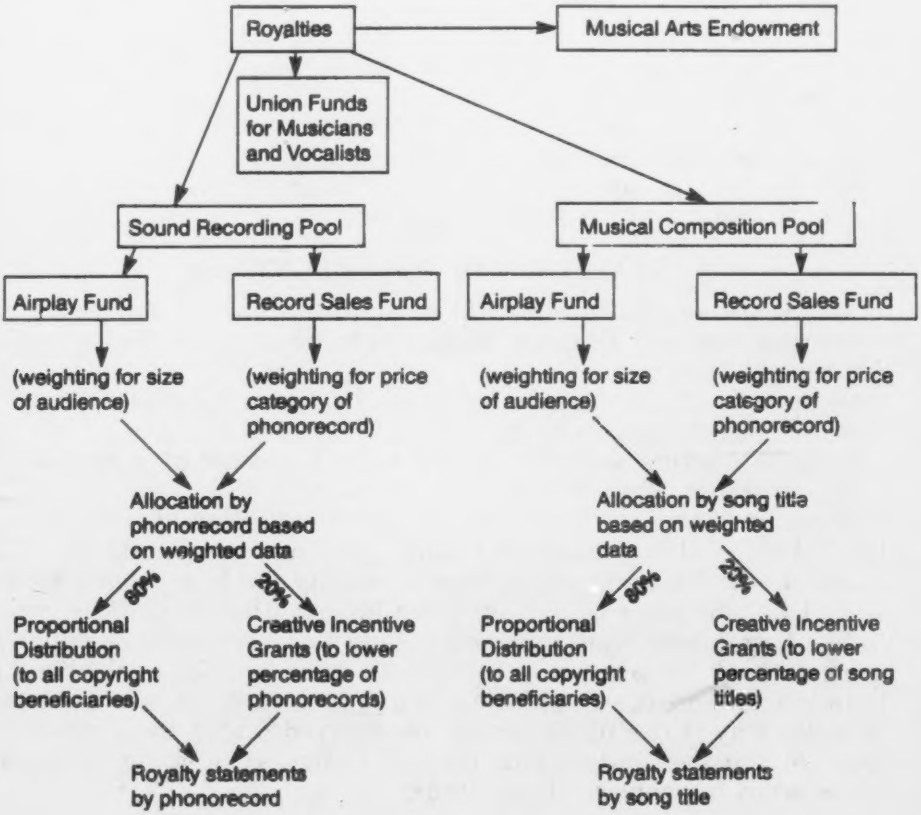
(weighting for size of audience)
(weighting for price category of phonorecord)
(weighting for size of audience)
(weighting for price category of phonorecord)
Allocation by phonorecord based on weighted data
Allocation by song title based on weighted data
80%
20%
80%
20%
Proportional Distribution (to all copyright beneficiaries)
Creative Incentive Grants (to lower percentage of phonorecords)
Proportional Distribution (to all copyright beneficiaries)
Creative Incentive Grants (to lower percentage of song titles)
Royalty statements by phonorecord
Royalty statements by song title

Once an allocation of the royalties generated by S. 1739 had been made along the lines set forth above, the organization charged with administration and supervision of the distribution system would prepare a proposal for submission to the Copyright Royalty Tribunal. That proposal would set forth the allocation formula, the procedures followed to reach that allocation formula, and the data on which it was based. Upon Tribunal approval of the allocation proposal, the supervising organization would also be charged with the disbursement of funds. Those disbursements would be shared by the copyright owners with all the others responsible for creating and producing the music. Royalties would thus flow, in the proportions identified above, from music publishers to composers and lyricists, and from record companies to recording artists. This flow in principle would replicate the flow of revenues from commercial recordings whose sales are displaced by home taping.

THE ROYALTY DISTRIBUTION SYSTEM


Royalties
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(weighting for size of audience)
(weighting for price category of phonorecord)
(weighting for size of audience)
(weighting for price category of phonorecord)
Allocation by phonorecord based on weighted data
Allocation by song title based on weighted data
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20%
80%
20%
Proportional Distribution (to all copyright beneficiaries)
Creative Incentive Grants (to lower percentage of phonorecords)
Proportional Distribution (to all copyright beneficiaries)
Creative Incentive Grants (to lower percentage of song titles)
Royalty statements by phonorecord
Royalty statements by song title

Senator **Mathias**. Thank you very much, Mr. Drake.

We have been joined by Senator Specter of Pennsylvania. He has not only joined us at this meeting, but also joined us as a member of the subcommittee. It is a pleasure to welcome him. He is under some time pressure and so I am going to yield to him.

OPENING STATEMENT OF HON. ARLEN SPECTER, A U.S. SENATOR FROM THE STATE OF PENNSYLVANIA

Senator **Specter**. Well, thank you very much, Mr. Chairman.

I am delighted to be here, delighted to be on this distinguished subcommittee. I regret that I cannot stay longer today, but I have a series of questions which I would like to submit for the record on this very important subject.

I thank you.

Senator **Mathias**. We will ask Mr. Drake and other witnesses if they will respond to your questions in writing and your questions and their responses will be made a part of the record.

Senator **Specter**. Thank you, Mr. Chairman.

Senator **Mathias**. Let me start with some questions. This is an extremely important subject which, as I said in my opening statement, is one of the basic issues that is raised with respect to this bill. I think it is important to be clear that we are on the same wavelength as far as the 80–20 plan is concerned.

Now, 100 percent of the artists who sell records or who have records that are played over the airwaves will share in the 80 percent of the royalties, but only those who earn the smallest amount of royalties, which is, as I understand it, about a third of the total number, will share in the remaining 20 percent. That is how you get the 80–20.

Will those who share in the 20 percent earn more than those who are compensated from the 80 percent pool?

Mr. **Drake**. Let me repeat the question, if I may.

Would you care to answer this, Bob?

STATEMENT OF ROBERT SUMMER

Mr. **Summer**. I believe I could respond to that.

We are assured that mathematically that could be prevented. That is not the intent.

Senator **Mathias**. You do not think that would happen?

Mr. **Summer**. No; we do not.

Senator **Mathias**. That is bound to be a matter of some concern.

Mr. **Summer**. That is right.

Senator **Mathias**. What about the Songwriters Guild Foundation? Under this general scheme, the Congress would be called upon to authorize the payment of a royalty fee to a private foundation. I do not have to call on your imagination to conjure up the kind of problems that that might engender somewhere down the road. I think we are going to need to know a good deal about the foundation, and the foundation is going to have to be accountable in some way if the funds which are derived under the authority of law go into the foundation. I think Congress is going to have to know what happens to these funds.

Mr. **Drake**. Well, in the first place, we have had our own experience on a more limited level in using funds that accrued to our foundation over the last 10 to 11 years. It is a going foundation. It is not just a figment of our imagination to be projected into the future. And we know how well it has worked on limited funds.

With a larger allocation, naturally we could attend to the needs of a great many more struggling—new struggling songwriters. We would, of course, like other elements of this entire plan be answerable to the Copyright Royalty Tribunal, which I would feel would question us vigorously as to our plans for distribution and our actual behavior and performance.

Senator **Mathias**. So the concept of some accountability does not concern you?

The foundation is prepared to render its accounts?

Mr. **Drake**. Indeed.

Senator **Mathias**. Yes.

Now, Mr. Summer, under the royalty distribution plan, the record companies would receive a smaller percentage of the royalty than they would have received from the proceeds of the displaced sale.

Why does the recording industry agree to narrow its slice of the pie?

Mr. **Summer**. The method that was employed took into account that the displaced sale, as an example, would not include a manufacturing cost. So there were different methods that were used to test the actual impact to each of those participating in the royalty system so that we could understand the true effect.

The record industry acknowledges this to be the true effect as it relates to their costs.

Senator **Mathias**. What Mr. Drake described as the Creative Incentive Grants—the 80-20 plan—would, in effect, weight the distribution scheme away from the superstars.

Am I correct?

Mr. **Summer**. That is correct.

Senator **Mathias**. It would also favor to some extent the less popular artists.

What is this going to do to companies in their decisions to record or not to record, or to invest in promotion of a lesser known artist or composer? Is it enough incentive to encourage taking that kind of a risk?

Mr. **Summer**. It is difficult to anticipate over time how the revenue flow would influence the decision to record. But certainly I would anticipate that the record company would be encouraged to record those forms of music that have a lesser audience.

Senator **Mathias**. Some of the small, independent companies have expressed concern about the way that the data underlying the royalty plan would be collected. They say, for example, that for some kinds of records, the traditional record store outlets are not all that important as far as sales are concerned. Many of their records are sold by mail order; they are sold at concerts and festivals.

Do the sales figures that are now compiled by the industry reflect accurately, or comprehend accurately, these less conventional outlets as well as the regular stores?

Mr. **Summer**. I believe we are dealing with a wholesale measure.

Senator **Mathias**. And you believe that measure would include less conventional outlets?

Mr. **Summer**. Yes, sir.

Senator **Mathias**. With regard to air play, what about the ASCAP and the BMI data bases? Do they adequately reflect the performances on noncommercial stations, stations which receive special treatment with respect to performance rights under section 118 of the copyright act?

Mr. **Drake**. There is in both ASCAP and BMI, I am sure the Senator is aware, a sampling system. It is not possible to actually record every performance of every song on every recording and every live performance in this vast country and its vast network of AM and FM stations. To do so would exhaust the entire revenues that these important organizations receive. Therefore they rely upon a sampling system. In a like way, we would reflect that sampling system in the evaluation of the performance of the phono record.

Senator **Mathias**. In the written testimony there is mention of a private sector administrative organization which might oversee the distribution of royalties collected under this legislation.

Is it the view of any member of this panel that the Copyright Royalty Tribunal should be relieved of responsibility? Or would this be a complementary organization?

Mr. Summer, do you have a view on that?

Mr. **Summer**. The tribunal, in my view, would continue in an oversight role but the actual administration of the system would be undertaken by an organization in the private sector. That is our suggestion.

Senator **Mathias**. Are you familiar with the way that ASCAP and BMI collect and catalog and make available the information on sound recordings that they acquire?

Mr. **Summer**. Yes.

Senator **Mathias**. Would that be available to any group attempting to determine who is entitled to what share of royalties?

Mr. **Summer**. You would have to negotiate access to that information. But it seems like a good path.

Senator **Mathias**. But it is not made public as a matter of course?

Mr. **Summer**. No.

Senator **Mathias**. Has it a commercial value?

Mr. **Summer**. It would be of value, yes.

Senator **Mathias**. Mr. Golodner, under the royalty distribution proposal that was just presented, the record companies seem to be willing to sacrifice a certain percentage of the royalties and hand that over to the unions and the artists, with whom, at least by the parties' testimony, they have been less than generous in the past.

Why do you think that they are willing to voluntarily turn over these funds to those for whom you speak here today?

STATEMENT OF JACK GOLODNER

Mr. **Golodner**. I do not think I would characterize this formula as a sacrifice on the part of the record companies.

Rather, it is a recognition of a partnership that exists in this industry, and a dependency on the creative artists for the future well-being of the industry.

What we are talking about here, Mr. Chairman, is music. Now music is not made by record dealers. Music is not made by lawyers. Music is not made by Japanese manufacturers of the hardware and equipment. These tapes, these wires, these metal pieces they made would be worthless in terms of the arts if it was not for the people I represent. That is what this issue is all about.

Senator **Mathias**. That really is what it is all about.

Mr. **Golodner**. Yes, it is. This is no sacrifice on the part of the record companies. We are not begging for anything. We are asking for our fair share for work that is being taken from us right now, stolen from us through the machine.

Now, this may seem to be very strong words. If we could back up a 100 years, I imagine there was some author who was making the same complaint about the printing press that we are making now about the ease with which people can copy our members' sounds.

Senator **Mathias**. The copyright law was a response to that complaint.

Mr. **Golodner**. Yes, it was, and it is not working today. It is not working, sir.

Senator **Mathias**. Well, we have moved through technology to the point where copyright protection is being eroded.

Mr. **Golodner**. I do not know of any other occupations that have been as affected by technological change in the last half century as those of the performing artists.

First, the recordings came out and sound movies and tens of thousands of musicians were displaced in our theaters. The juke box displaced tens of thousands more. We said that was progress, and it was, and the consumer benefited.

Then broadcasting was linked to the high fidelity recording. And many, many more thousands of American performers were displaced from our radio stations. In a peculiar way, it comes now full circle because those recordings on the air are now being taped at home, and are cutting into the sales of the recording artists and into the sales of those who are purveying those records.

I do not see how this legislation can hurt a dealer in sound recordings. If he is in the business of selling sound recordings, he must put some of that money back into the creative source so that he has more new artists, more recordings coming out to sell. I do not see where any harm has been established by this legislation for these people.

But our people are hurting. They are being harmed not only in terms of employment but in terms of income. We are not asking for their jobs back. We are asking Congress and the American public to say "yes, we are benefiting from this technology and we would like you—the artist—to share in it a little bit." This is necessary because the Japanese manufacturers of the taping equipment have turned a deaf ear to America's performing artists and will not voluntarily share their largesse.

Senator **Mathias**. What about the union funds that, under this plan, amount to approximately 2 percent of the royalties collected?

How do you think that these funds would be employed to encourage creativity and provide incentives for musical diversity?

Mr. **Golodner**. We have some experience in this, Mr. Chairman.

With regard to the musicians there was a fund established which is fed by moneys derived from the sale of records. This is the Music Performance Trust Fund. It was established back in the 1940's, so there is quite a history of this, and it has amounted over the years to as much as $16 or $17 million a year in the good years.

This money benefits us all because it pays for free concerts in the park, and civic parades, where the musicians may be professional musicians but the fund is paying for them. The fund is also used for school concerts; it is used for concerts in our recreational areas; wherever music is free and open to the general public, you will probably find MPTF providing some of the moneys for it.

This accomplishes two things. It reminds the American public of the value of the live music, and it encourages an interest in it. Second, it provides employment for those musicians who have been displaced by the various technological changes that I have mentioned.

Later on, about the 1960's, another fund, the Special Payments Fund, was established, which also is based on record sales. This money goes directly to the artists that made the recordings, according to a rather complicated formula. But, basically, it is designed to provide additional compensation for those musicians who are making these records so they can share in the sales revenue along with the record companies and others.

We contemplate that the moneys which will be distributed under what is proposed in S. 1739 will be handled in much the same way. They will be used to compensate those musicians who have been harmed economically by the increasing practice of taping and to acknowledge their invaluable contribution to the very profitable business of manufacturing and selling recording devices and blank tapes.

Senator **Mathias**. What about the difference between the stars and small musicians?

Mr. **Golodner**. Well, as the funds now operate, as I understand it that these unions operate, no distinction is made.

Senator **Mathias**. But under this distribution plan, there is an attempt under the 80-20 formula to address the difference between the stars and lesser known musicians. I think the stars are going to benefit under anything that happens in life.

But does this also give enough recognition to the so-called struggling artists?

Mr. **Golodner**. We think that the plan that has been proposed here does.

As far as the moneys that will be redistributed to the vocalists and musicians and other performers on sound recordings, that 2 percent will be taken out of the 80 percent and the 20 percent. So we would share 2 percent of the 100 percent in the pool. And the creative incentive grant proposal is one which would not affect our distribution at any rate.

Senator **Mathias**. I have some additional questions, but as in the case of the last panel, I think if we ask them all, we will impinge upon the time of the last panel. It is an important panel, and one that I want to make sure has adequate time to present its case.

So if I may, I will ask you to respond in writing to some additional questions. Other members of the committee may also have some questions they want to pose to you.

[Mr. Golodner's statement and responses to written questions, subsequently received for the record, follow:]

STATEMENT
OF
JACK GOLODNER, DIRECTOR
DEPARTMENT FOR PROFESSIONAL EMPLOYEES, AFL-CIO

FOR THE
SUBCOMMITTEE ON PATENTS, COPYRIGHTS AND TRADEMARKS
OF THE
SENATE COMMITTEE ON THE JUDICIARY
IN SUPPORT OF
THE HOME AUDIO RECORDING ACT
S. 1739

In am Jack Golodner, Director of the Department for Professional Employees (DPE), AFL-CIO. I want to convey to the Subcommittee the strong support of the AFL-CIO[1] and of the DPE for the Home Audio Recording Act -- S. 1739.

But before proceeding to a discussion of the Home Audio Recording Act, perhaps a few words about the DPE might be useful. One of the constitutional components of the AFL-CIO, the DPE brings together 27 national and international unions (list attached) which represent in their membership approximately 3 million professional, technical, and highly skilled white collar workers. They include the performing artists — musicians, singers, and other performers -- as well as the technicians and craftspersons who make up the work force of the sound recording industry. They also include teachers, librarians, nurses, engineers, pharmacists, athletes, scientists, etc. Indeed, every major profession and technical occupation is represented in the ranks of our affiliated organizations. Many of these individuals engage in the home taping of sound recordings, others are purchasers of records and pre-recorded audio tapes, and most engage in both of these activities. Thus, I think it is fair to say that our strong support for the Home Audio Recording Act is representative of both the creators and consumers of sound recordings. We believe that the legislation is a fair and equitable resolution of all the interests affected by it.

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[1] A copy of the resolution endorsing the Home Audio Recording Act by the Sixteenth Constitutional Convention of the AFL-CIO held in Anaheim, California, from October 28-31, 1985, is attached.

Home audio taping has been going on for some time in the United States. Taping off-the-air and the taping of records and pre-recorded tapes are all commonplace today. Copied audio tapes are libraried, loaned, exchanged and given away. No one seriously questions that the sound recording industry is losing money from the unauthorized taping of its copyrighted sound recordings. The only dispute regards the extent of the harm. Is it measured in billions or merely hundreds of millions of dollars each year.

Economic Arguments Ignore Plight of American Performing Artists and Supporting Personnel

Those who oppose the legislation are attempting to portray it as a cynical grab for more money by wealthy recording artists and record companies deserving of no further compensation for the unauthorized taping of their copyrighted sound recordings. In the main, the opposition to the legislation is coming from the Washington based representatives of the foreign manufacturers of home recording equipment who pretend to represent the interests of Americans who engage in home taping while in fact seeking to sustain the enormous profits of their principals. They have so distorted the issue that whether or not the Home Audio Recording Act should be enacted now would appear to turn on the profitability of the record companies. A means test, if you would. But in posing the issue those who oppose the legislation have conveniently chosen to ignore the financial plight of the backup musicians, singers, and other performers as well as the craft and technical workers who make up the bulk of the work force in the sound recording industry.

A sense of the economic plight of America's performing artists is provided by two studies funded by the U.S. Department of Labor, the National Endowment for the Arts, and the Ford Foundation. These studies, the latest available on the subject, document the high unemployment, poor pay, and lengthy and expensive education and training which mark the performer's career. The following quotations from the reports on these studies, though requiring adjustments of the earnings cited to reflect the inflation which has occurred since the studies were completed, paint an accurate picture of what most performing artists endure, including most of those who work in the sound recording industry.

> The jobs of performing artists tend to be more intermittent than those of other workers; their periods without work more numerous and long-lasting; and their pay well below that of other professionals. (p. 1).
>
> Income and Earnings
>
> Performers' individual earnings are also considerably lower than those of workers employed in similar occupations in the workforce. For male performers, earnings fell between $6,000 and $10,000 below the 1980 median earnings of male professional, technical, and kindred workers; for female performers, the comparable earning gap was between $1,000 and $5,000. (p. 9).
>
> Unemployment
>
> Performing artists are much more prone to unemployment than members of the civilian labor force as a whole. Just 18 percent of persons in the civilian labor force experienced some unemployment during 1980 — well below the 76 percent of dancers, 67 percent of actors, 61 percent of singers, 35 percent of musicians, and 21 percent of performers in broadcasting occupations.
>
> * * * * *
>
> Their (performing artists) unemployment experience is severe both in terms of the number of spells of unemployment and the length of time they are out of work. While 15 percent of all unemployed workers in the labor force had three or more jobless spells in 1980, for unemployed performing artists the proportion was over one-third. .... (p. 5).[2]

The earlier report makes it clear that these conditions prevail as well among performers in the recording industry.

> Returning to the two issues raised at the beginning, are performers already benefitting from the existing procedures in regard to the production and sales of records and are they receiving adequate compensation for their efforts, survey data indicate negative answers to both questions. Only a small proportion of those engaged in the production of sound recordings receive any financial benefits from the sale of those records. In the three groups most affected only 23 percent of the musicians benefit from sales, 5 percent of the musical artists and 17 percent of the radio and TV artists. Furthermore, annual earnings of performers as a group are generally low, with almost a third of the musicians and two fifths of the musical artists and radio and TV artists earning $7,000 a year or less.[3]

And while the circumstances of the technicians and craftspersons who work in the recording industry are not as bleak as those of the backup performers on sound recordings they are far from being lavish. Further exacerbating the problem has been the steep decline in employment in the sound recording industry since the onset of home taping.

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[2] Working and Not Working in the Performing Arts: A Survey of Employment, Underemployment and Unemployment Among Performing Artists in 1980. Ruttenberg, Friedman, Kilgallon. Gutchess & Associates, Inc. December 31, 1981. (Funded by grants from the National Endowment for the Arts, the U.S. Department of Labor, and the Ford Foundation.)

[3] Performance Rights in Sound Recordings, Subcommittee on Courts, Civil Liberties and the Administration of Justice, U.S. House of Representatives, 95th Congress, Second Session, June 1978. Committee Print No. 15., pp. 119-120.

The Issue is Equity and Integrity of Copyright System

But the profitability or lack thereof of record companies and the plight of performing artists is not the central point here. What is placed in issue by the unauthorized taping of copyrighted sound recordings is the integrity of our system of copyright and whether the property rights of copyright owners will be honored.

What is placed at risk is a copyright system on which whole industries are based which according to the latest available data contribute over $55 billion (2.8%) to the gross annual national product, employ more than 2 million people, and are some of the few industries in our economy making a substantial positive contribution to our balance of trade.

From the time when taping equipment first became available with which acceptable copies of musical recordings could be made, it was recognized that the property rights of the copyright owners of those recordings were being violated. As in the case of reprography and other recent technological innovations, the question is not what rights does the copyright owner have, but rather how can those rights be enforced. Taking place as it does in the home, that bastion of rights under our laws, audio taping of copyrighted sound recordings has presented even more difficult problems for public policy makers.

But the Home Audio Recording Act is a workable affirmation and extension of the copyright law. As does the copyright law, it acknowledges that there is no such thing as a free lunch and the truth of the admonition that the piper must be paid if he is to continue playing. And it upholds the constitutional principle that private property cannot be taken from its owner without fair compensation.

In return for a modest royalty fee on blank audio tapes used for recording copyrighted sound recordings and on audio recording devices used for such purposes individuals are permitted to tape copyrighted sound recordings for their personal use. The revenues from these royalty fees will be distributed among the copyright owners of the sound recordings which are taped. What could be more fair and equitable.

I urge the prompt enactment of the Home Audio Recording Act.

AFFILIATES OF THE DEPARTMENT FOR PROFESSIONAL EMPLOYEES, AFL-CIO

Actors' Equity Association

American Federation of Government Employees

American Federation of Musicians

American Federation of State, County and Municipal Employees

American Federation of Teachers

American Federation of Television and Radio Artists

American Guild of Musical Artists

Association of Theatrical Press Agents and Managers

Brotherhood of Railway and Airline Clerks

Communications Workers of America

Federation of Professional Athletes

International Alliance of Theatrical Stage Employes and Moving Picture Machine Operators

International Association of Machinists

International Brotherhood of Electrical Workers

International Federation of Professional and Technical Engineers

International Union of Electronic, Electrical, Technical, Salaried and Machine Workers

International Union of Operating Engineers

International Union, United Automobile, Aerospace & Implement Workers of America

National Association of Broadcast Employees and Technicians

National Union of Hospital & Health Care Employees

Office and Professional Employees International Union

Retail, Wholesale and Department Store Union

Screen Actors Guild

Seafarers International Union

Service Employees International Union

United Association of Journeymen Plumbers

United Food and Commercial Workers

RESOLUTION OF THE AFL-CIO

ADOPTED AT ITS SIXTEENTH CONSTITUTIONAL CONVENTION

IN OCTOBER 1985

Preserving the American Copyright System and Jobs in the Performing Arts

RESOLUTION NO. 250—By the Department of Professional Employees.

The public and artists, performers, and supporting craft and technical workers in the performing arts have a stake in enactment of the Home Audio Recording Act which has been introduced in the Congress.

This legislation responds to the widespread unauthorized taping of copyrighted sound recordings which deprives artists, performers, and supporting craft and technical workers who produce such recordings of rightful recompense for their labor. Such taping also increases the cost of copyrighted sound recordings to individuals who purchase them, and limits the diversity of sound recordings which are produced.

The Home Audio Recording Act would:

- Exempt any individuals who copied a copyrighted sound recording for personal use from copyright infringement liability; and

- Require importers and manufacturers of audio recording equipment and blank tapes which are used for the home recording of copyrighted sound recordings to pay a reasonable royalty fee which would be distributed among copyright owners of sound recordings which are taped in the home.

The Home Audio Recording Act is a fair and equitable resolution of the home audio taping issue. It will permit the consumer to benefit from a continuing diversity of sound recordings as well as improved audio recording devices and tapes. At the same time the performers, writers, technicians and crafts people who produce sound recordings will be fairly compensated for this use of their work; therefore, be it

RESOLVED: That the AFL-CIO endorses the Home Audio Recording Act and will work to secure its enactment into law.

DPE

Department for Professional Employees, AFL-CIO
815 16th Street, N.W., Washington, D.C. 20006 Phone 202/638-0320

April 22, 1986

Senator Charles McC. Mathias, Jr.
Chairman
Subcommittee on Patents, Copyrights, and Trademarks
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Chairman Mathias:

I write in response to your letter of April 10, 1986, in which you ask that I answer the following questions submitted by Senator Specter in connection with the hearing on March 25, 1986, on the Home Audio Recording Act (S. 1739):

QUESTION

How did you arrive at the distribution of monies proposal which you present here today?

RESPONSE

The distribution of monies proposal made in the joint statement presented to the Subcommittee on March 25, 1986, is based on a number of different factors, including the revenues historically and presently enjoyed by each music constituency from the sale of sound recordings; and the public policy objectives of the Home Audio Recording Act (the "Act"). But as the table on page 25 of the joint statement and accompanying text indicate, the percentages of royalties payable to all but one group of recipients under the Act would be increased over the share of revenues each group presently receives from the sale of records. The one group that would receive less under the Act than from the sale of records would be the record companies. This diminution in the share payable to record companies under the Act recognizes both that certain manufacturing and distribution costs normally borne by the record companies may not be incurred when a sale is displaced by home taping, and that the goals of the legislation, which include nurturing new talent and new music, can be better served if artists and songwriters are given an enhanced share.

QUESTION

Which groups were represented in the development of this proposal?

RESPONSE

I was not a party to the negotiations leading to the proposed royalty distribution plan. I am informed, however, that the President of the American Federation of Musicians (AFM) and the National Executive Secretary of the American Federation of Television and Radio Artists (AFTRA) participated in discussions with the President of the Recording Industry Association of America (RIAA) with regard to the proposal. The AFM and AFTRA are affiliates of this Department. Together, these organizations represent the overwhelming preponderance of musicians, vocalists and actors who record in this country. I believe that representatives of all other groups affected by the proposal were involved in similar discussions or negotiations with regard to it, but I have no personal knowledge of those discussions or who was involved in them.

QUESTION

How did you feel that the plan meets the two criteria of (1) ensuring compensation to copyright beneficiaries, and (2) promoting the creation and dissemination of new music?

RESPONSE

The plan ensures that copyright beneficiaries will be compensated for home taping while promoting the creation and dissemination of new music. First, the plan provides that the bulk of the royalty pool generated under the Act will be distributed to all of the copyright beneficiaries in proportion to the airplay and sales of their work. Because airplay and record sales data show which albums and tunes are most in public demand, these data can be used to identify the music that is most taped, and thus to ensure that the bulk of the royalties will be distributed so as to reflect the extent and pattern of home taping.

The distribution plan also promotes the creation and dissemination of new music in two ways. First, it provides for a Musical Arts Endowment which would receive two percent of the royalties generated by the Act. One half of the funds of the Musical Arts Endowment would be received by the Songwriters Guild Foundation to assist its program for developing and encouraging new lyricists and composers.

The remaining half of the funds of the Musical Arts Endowment would be received by the National Endowment for the Arts (established by the National Foundation on the Arts and the Humanities Act of 1965 — Public Law #89-209) to support the education and training of vocalists and musicians. Thus the Musical Arts Endowment would promote the creation and dissemination of new music by fostering the education, training, and careers of those who would compose it and the lyricists who would write the words to accompany that music, as well as of the vocalists and musicians who would perform it.

Second, the plan provides for Creative Incentive Grants which would be made to those copyright beneficiaries whose recorded works are not in substantial public demand, and thus, are most in need of added financial incentive. These, we believe, would include almost all of those who create, perform, and record new music for which no general public demand has yet developed. Jazz, folk, and some contemporary classical music are among those art forms which I believe are in need of such added encouragement.

CONCLUSION

I trust that my responses to these questions posed by Senator Specter are responsive and provide all the information which was desired. I appreciate the opportunity to have appeared and testified before the Subcommittee on the Home Audio Recording Act and urge the Subcommittee to report that legislation favorably at the earliest opportunity.

Sincerely,

Jack Golodner
Director

Senator MATHIAS. Mr. Drake, let me say that your testimony comes with a very high level of credibility because you are absolutely right.

When I was 17, it was a very good year. [Laughter.]

Thank you very much for being here.

Mr. GOLODNER. We thank you.

Mr. SUMMER. Thank you, sir.

Mr. DRAKE. Thank you, sir.

Senator MATHIAS. Now we have the final panel this morning which consists of some figures well known in this room: Charles Ferris, Audio Recording Rights Coalition, and Barry Mann, manager of David Mann's Audio, Philadelphia, PA.

Mr. Ferris.

STATEMENTS OF PANEL CONSISTING OF CHARLES D. FERRIS, ATTORNEY, REPRESENTING AUDIO RECORDING RIGHTS COALITION, WASHINGTON, DC; AND BARRY MANN, PRINCIPLE, DAVID MANN AUDIO, PHILADELPHIA, PA

Mr. FERRIS. Mr. Chairman, our coalition has been before your subcommittee several times in the past few years. We have vigorously stated our opposition to the various proposals to place royalty taxes on recorders and blank tape. Today you have invited us to appear to comment on one aspect of the royalty tax bill, S. 1739, that purports to provide an exemption to the royalty tax.

Mr. Chairman, the only reason opponents seek a discussion on so-called exemptions to S. 1739 is because focusing on this technological fix bypasses the central issue: is home taping a problem that needs a solution? Talk of exempting is really a backdoor effort to tax recorders and blank tape so that people will pay more and receive less.

The record industry is booming, and the current health of the industry is very much a result of the portable tape players and compact disc technology introduced by the manufacturers who are being attacked by this legislation. It is these same manufacturers that invested millions to develop the recording technology, including the compact disc, that permits the recording industry and the artists that Mr. Golodner represents to earn their hundreds of millions of dollars each year. At least as good a case can be made that the recording industry should be paying a royalty tax to these manufacturers each time one of their recordings is played on these machines as can be made that the manufacturers should pay a royalty to the record companies. The unprecedented revenues enjoyed by the record industry are thanks not only to these manufacturers, but also to the buying habits of home tapers who are the record companies' best customers. In seeking this legislation, the record companies are attacking the very people who have helped prosper, the hardware manufacturers and the record buyers.

According to S. 1739, any hardware "which incorporates a decoder or similar mechanism that prevents the device from reproducing" is exempt from the royalty tax.

The purpose of this technology purportedly is not to wipe out all home taping. In fact, the legislation recognizes by exempting home taping from copyright infringement—an exemption consumers do not need—that consumers should be able to tape. The recording industry, however, wants to make people pay for the right to tape their own records in their own homes for their own personal use. So how would this work?

First, with respect to the hardware, we hear this morning that manufacturers have a choice. If they want their customers to avoid paying a hardware royalty tax, they can make machines with the decoder technology. According to the bill, such machines are exempt from the tax. All other audio recorders which will be able to tape would be subject to the royalty tax.

Second, on the software side, companies would begin producing encoded records, tapes and discs which, if played on a machine with a decoder chip, could not be taped. But what about the owners of machines with chips who decide they want to tape? They will be able to do so, but only for a price. The record companies suggest they will also sell unencoded software to consumers who have purchased machines with chips in the form of records, tapes, and discs without the signals. In other words, the same products that are available today. The record companies, however, will surely then charge more for the unencoded products as a fee for the right to tape it.

And it was interesting, Mr. Chairman, that Mr. Gortikov was unable to answer how much that premium would be.

The record companies get paid up front then from the tax on the machines that can tape, and they get paid at the back when they sell the higher priced software that can be taped.

But let us not forget that the consumers pay yet again when they buy a blank tape because the legislation taxes blank tape at a penny per minute. Seems like a double, if not a triple, whammy to me, Mr. Chairman. This is no technological exemption to a tax. It is just another kind of tax levied technologically. A tax on top of a tax, if you will.

In addition to forcing a double tax on consumers, the decoder chip technology would impose on retailers the heavy burdens of stocking dual hardware and software inventories. Machines with decoder chips, machines without, and software in six formats would all be part of the new marketplace the legislation would create.

In a moment, Barry Mann, a retailer, will discuss some of the problems he foresees.

Now, with two kinds of software and now two kinds of hardware, how will consumers decide what to buy? If they buy decoder chip machines, will the record companies supply adequate inventories of unencoded software at reasonable prices? Will they effectively take away the now well-established and perfectly legal right to tape by creating software scarcities that will force consumers to pay premium prices for exercising that right?

With respect to the impact of the decoder chip technology on hardware, the impact is potentially even more devastating. Will consumers pay whopping royalty taxes up front for machines with capabilities similar to those available now? Will the Government continue to meddle in the market and try to set the price of hardware without encoder chips?

What really will happen to the price of the two kinds of software? Are the record companies going to be able to charge consumers whatever they want for the right to tape? Or will the Government intercede to protect people who have committed to one kind of machine only to find the software prices are shifting? What will happen to the 138.2 million recorders people already own? These machines can take any software because the signals have no effect on them. Why would someone buy a new one that is less capable than the one he already has? The repair business may do very well, Mr. Chairman, but what will happen to the sales of hardware?

I cannot answer these questions. Nor need you answer them, Mr. Chairman, if you just consider the central question: is it fair or necessary to subject consumers to this tax and these chips? If you look at how recorders are really used and how much and why people tape at home, you will see that there is no need for this legislation.

Studies show that by far the most common use of a recorder is to play back, not to record.

Mr. Gortikov of the recording industry has, on several occasions, smashed up a blank cassette before this subcommittee to show that there is no inherent value inside. Mr. Golodner today made this same point about the metal and the wires having no inherent value.

Well, people have not been buying Mr. Gortikov's prerecorded cassettes or listening to Mr. Golodner's artists by holding them close to their ears. The ascendancy of the prerecorded tape, which has occurred in lockstep with the industry's return to prosperity, has happened because people have recorders at home and they have portable players everywhere else.

Typical taping behavior is beneficial rather than costly. All the anecdotes about kids buying records and making copies for their friends are just that, anecdotes, and they tend to obscure the concrete, verifiable truth. Every study ever done, whether sponsored by our group, the record industry, or someone else has shown that people who do the most home taping own the largest collections of records and prerecorded tapes.

The comprehensive survey conducted by Yankelovich, Skelly and White, a part of this record at the previous hearing, found that of the tapes people have that were made from prerecorded music, a majority of records and tapes are made from the prerecorded music in the taper's own collection. In other words, with respect to a majority of tapes that people made at home, they bought the source material themselves, they kept it, they copied it, and they kept the copy too. Why? The study also asked that question too.

Of the tapes in peoples' collections, fully two-thirds contained selections from various albums, rather than complete albums. People made such tapes to have more convenient access to their favorites as well as to take in their car or at the beach. Can anyone doubt that this trend to portable music has helped sell records and tapes?

The other obvious reason for recording from one's own records is to preserve them. It is the real music lover, Mr. Chairman, who buys a record, then wants to make a high quality tape of it, of higher quality than he can buy on prerecorded cassettes before the inevitable scratches and pops show up.

I have engaged in this short analysis, Mr. Chairman, of taping behavior for two reasons. First, it shows that even when uses that do not involve prerecorded music are not considered, the royalty tax is a penalty on good customers rather than the solution to any problem.

Second, it allows me to demonstrate that the decoder chip provision, if it causes recorder manufacturers to choose between selling recorders with decoder chips or selling higher priced ones without them, has the same problems as the tax itself. It attacks the typical good taper who seeks quality, portability and convenience, and leaves unpenalized the kids who allegedly tape only to save money, who continue their practices so long as they have an old recorder handy.

Mr. Chairman, in all seriousness, any provision that requires decoder chips penalizes people for not having them, or makes recorders without them more expensive is the consumer electronics version of the neutron bomb. It wipes out the people interested in buying music and making quality recordings for their personal use, while it leaves totally unaffected the very few who are said to be creating a problem for the recording industry.

Mr. Chairman, in our view, the fundamental misconception about home taping is that there is any problem that needs a solution. Our coalition has fought every royalty tax proposal, pointing out the inherent problems of unfairness and overbreadth. Apparently, in moving on to decoder chip ideas, the subcommittee is looking for a magic bullet. If this system is one, it is aimed at all the wrong people.

The manufacturers who do not wish to adulterate their products, and the retailers who do not wish to sell such products, both are sincere in their belief that the hardware and software industries are mutually and equally beneficial. If anything, new technology, recently introduced by the hardware manufacturers, has provided out-of-scale benefits to the software proprietors who are keen enough to take advantage.

In baseball they say, Mr. Chairman, that sometimes the best trade is the one you do not make. I respectfully submit that in home recording, the best solution is to leave well enough alone.

Thank you.

[The prepared statement of Mr. Ferris follows:]

PREPARED STATEMENT OF CHARLES D. FERRIS

Mr. Chairman and members of the Subcommittee, my name is Charles D. Ferris. I am an attorney in Washington, D.C. I am here today representing the Audio Recording Rights Coalition and the millions of Americans who own and use audio recorders and tapes in their homes.

The Audio Recording Rights Coalition includes companies that are involved in the manufacture, sale, and distribution of audio cassette recorders and audio tape, and related equipment. They include Tandy Corporation, 3M, G.E., Pfizer, DuPont, Memtek Products, Maxell, J.C. Penney, Sears, Roebuck & Co., Sony Corporation of America, and Matsushita Electric Corporation of America. Our membership includes many prominent trade associations, such as the Electronic Industries Association, the American Retail Federation, the National Retail Merchants Association, along with various consumer groups, thousands of individual retailers, educational organizations, and the American Council for the Blind.

Mr. Chairman, our Coalition has been before your Subcommittee several times in the past few years. We have vigorously stated our opposition to various proposals to place royalty taxes on recorders and blank tape that are used by consumers at home for a myriad of purposes. You have invited us to appear today to comment on one aspect of the royalty tax bill, S. 1739, that purports to provide a quote, exemption, unquote to the royalty tax.

This is no exemption. First, the legislation, no matter how it is packaged, removes rights that consumers have enjoyed for years and then makes them pay for those rights.

Second, what we're really talking about here is a double tax. Third, and perhaps worst, this technological interventionism will distort both the hardware and software markets.

Mr. Chairman, the only reason proponents seek a discussion on so-called exemptions to S. 1739 is because focusing on a technological "fix" bypasses the central issue: is home taping a problem that needs a solution? All the hearings on this central question have revealed only that the record companies want a subsidy in good times and in bad times. Any basis for such a subsidy is dismally wanting. In fact, the record to date shows that any legislative fiat would be unnecessary, unwarranted, and unfair. Talk of "exempting" is really a bootstrap effort to tax recorders and blank tape so that people will pay more and receive less.

If I may put this in context, home taping is legal. There is no case, no legislative history, nor any other statement - other than that of the recording industry - to the contrary. The proponents of the Home Audio Recording Act are trying to change the law. These proponents of change have the burden to show that such changes are necessary. They have not met that burden. The copyright laws continue to maintain a fair balance between the public's access to creative works and the artists' needs for continued incentives for creativity. The record industry is booming and new acts and new music are continually being introduced.[1] Contrary to claims by RIAA, home taping is not killing the music industry. We have shown that much of home taping has nothing to do with prerecorded music. We have testified about the stimulative effect home taping of prerecorded music has on record sales. We have explained that new technology has been a boon to the record industry.

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[1] CBS Records projects total retail sales for the U.S. recording industry will top $4.52 billion mark in 1986, a hike of 3.5% over 1985's estimated $4.37 billion. Billboard, March 22, 1986, p. 3.

The current health of the industry is very much a result of the portable tape players and compact disc technology introduced by the manufacturers who are being attacked by this legislation. It is these same manufacturers that invested millions to develop the recording technology, including the compact disc, that permits the recording industry to earn their hundreds of millions each year. At least as good a case can be made that the recording industry should be paying a royalty tax to these manufacturers each time one of their recordings is played on these machines as can be made that the manufacturers should pay a royalty to the record companies. The unprecedented revenues enjoyed by the record industry are thanks not only to these manufacturers, but also to the buying habits of home tapers who are the record companies best customers. In seeking this legislation, the record companies are attacking the very people who have helped them prosper: the hardware manufacturers and record buyers.

Until some need for the basic legislation is established, discussions of exemptions are diversionary at best. I am concerned, Mr. Chairman, that these hearings not mislead the Congress into thinking that the anti-duping technology will somehow obviate the need to deal with the fundamental points I just set forth.

Congress should not lose sight of the fact that the application of this decoder chip technology assumes the passage of the Home Audio Recording Act. According to S. 1739, any hardware "which incorporates a decoder or similar mechanism that prevents the device from reproducing" is exempt from the royalty tax. All other hardware and all blank tape would still be taxed. In spite of claims that this technology is a "marketplace solution" to home taping, the fact is that without a tax, this technology would never be adopted by the market.

Forcing this technology on markets which otherwise wouldn't tolerate it will have all sorts of commercial and practical ramifications far beyond those Congress might expect. Again, recognizing that the decoder technology is only the fly on the camel's back in this debate, let me tell you how I think it would work commercially.

The purpose of the technology purportedly is not to wipe out all home taping. In fact, the legislation recognizes by exempting home taping from copyright infringement (an "exemption" we don't need) that consumers should be able to tape. The recording industry, however, wants to make people pay for the right to tape their own records. So how would this work?

First, with respect to hardware, manufacturers have a choice. If they want their customers to avoid paying a hardware royalty tax, they can make machines with the decoder technology. According to the bill, such machines are exempt from the tax. All other audio recorders, which will be able to tape, would be subject to the royalty tax.

Second, on the software side, the recording companies would begin producing encoded records, tapes, and discs, which, if played on a machine with a decoder chip, could not be taped. But, what about owners of machines with chips who decide they want to tape? They will be able to do so, but only for a price. The record companies suggest they will also sell unencoded software to consumers who have purchased machines with chips, in the form of records, tapes, and discs without the signals--in other words, the same products that are available today. The record companies, however, will surely then charge more for the unencoded products, as a fee for the right to tape it. The record companies get paid up front from the tax on machines that can tape; they get paid at the back end when they sell the higher-priced software that can be taped.

No matter whether a consumer buys a taxed machine or expensive software, the consumer ends up paying the record companies for the right to tape records he has already bought. But let's not forget that consumers pay yet again when they pay the tax on blank tape because the legislation taxes blank tape at a penny per minute. Seems like a double - if not a triple - whammy to me. This is no technological exemption to a tax, it is just another kind of tax levied technologically. A tax on top of a tax, if you will.

In addition to forcing a double tax on consumers, the decoder chip technology would impose on retailers the heavy burdens of stocking dual hardware and software inventories; the proposal is so onerous in this respect that it reminds me of the retailer outcry when this Subcommittee was considering video first sale legislation in the last Congress. Machines with decoder chips, machines without, and software in six formats, would all be part of the new marketplace the legislation would create. In a moment, Barry Mann, a retailer, will discuss some of the problems he foresees.

In addition to the dual inventory scheme that the new technology would mandate, it also raises a series of important - and unexplored - questions about how software and hardware would be priced. I submit, Mr. Chairman, that the decoder chip proposal will devastate two now healthy markets.

With two kinds of software and two kinds of hardware, how will consumers decide what to buy? If they buy decoder chip machines, will the record companies supply adequate inventories of unencoded software at reasonable prices? Will they effectively take away the now well-established, and perfectly legal, right to tape by creating software scarcities that will force consumers to pay premium prices for exercising that right?

With respect to the impact of the decoder chip technology on hardware, the impact is potentially even more devastating. Will consumers pay whopping royalty taxes up front for machines with capabilities similar to those available now? Will the government continue to meddle with the market and try to set the price of hardware without encoder chips?

What will really happen to the price of the two kinds of software? Are the record companies going to be able to charge consumers whatever they want to for the right to tape? Or will the government intercede to protect people who have committed to one kind of machine only to find the software prices shifting? What will happen to the 138.2 million recorders people already own? These machines can tape any software because the signals have no effect on them. Why would someone buy a new one that is less capable than one he already has? The repair business may do very well, but what will happen to sales of hardware?

I can't answer these questions. Nor need you answer them if you just consider the central question: is it fair or necessary to subject consumers to this tax and these chips? If you look at how recorders are really used and how much and why people tape at home, you will see there is no need for this legislation.

Typical Home Use of Recorders Is Greatly Beneficial to the Record Industry

In the course of focusing on the decoder chip technology, we don't want you to lose sight of the basics. The entire concept of a royalty tax is flawed because recorders and blank tape are used only about half the time to record prerecorded music. The decoder chip technology is fatally overbroad because it misses an equally fundamental point: even when only prerecorded material is considered, the basic, typical and fundamental uses of recorders and tape benefit the recording industry. As a Member of Congress once observed, if all the country's tape recorders were somehow collected and dumped in Lake Michigan, it would be in the interests of the software suppliers to fish them out and return them to their owners.

Recorders Are Most Commonly Used As Players

Studies show that, by far, the most common use of a recorder is as a player. This follows a familiar pattern--a new recording device frightens program suppliers, until they learn how to capture it as a market of their own. As in the case of video recorders and personal computers, a multi-billion dollar software industry emerges, and the profits flow to those who recognize it first and most keenly. This, Mr. Chairman, is the marketplace "solution."

Mr. Gortikov, of the Recording Industry Association of America, has on several occasions smashed up a blank cassette, to show that there is no inherent value inside.

Well, people haven't been buying his companies' prerecorded cassettes and listening to them by holding them close to their ears. The ascendancy of the prerecorded tape, which has occurred in lockstep with the industry's return to prosperity, has happened because people have recorders at home and they have portable recorders and players everywhere else.

Studies also show that, even though they will wind up using them mostly for playback, people want their home units to be recorders, as well as players. The consumer values his freedom and independence. To enjoy the huge new market served by prerecorded tape, is this too big a price for the record companies to pay? The fact is, the recording capability of tape recorders is typically not a cost to the record companies at all. Rather, it is likely to be a benefit. Forcing manufacturers to sell "recorders" that don't record would be simply an outrage.

Typical Taping Behavior Is Beneficial Rather Than Costly

All the anecdotes about "kids" buying records and making copies for their friends are just that--anecdotes--and they tend to obscure the concrete, verifiable truth. Every study ever done, whether sponsored by our group, the record industry, or someone else, has shown that people who do the most home taping own the largest collections of records and prerecorded tapes.

We have confirmed, and presented the evidence to this Subcommittee, that typical taping behavior does not involve making copies for others. The comprehensive survey conducted by Yankelovich, Skelly and White found that of the tapes people have that were made from prerecorded music, a majority of records and tapes are made from prerecorded music in a taper's own collection. In other words, with respect to the majority of tapes that people made at home, they bought the source material themselves, they kept it, they copied it, and they kept the copy too. Why? We asked them that also.

Of the tapes in peoples' collections, fully two-thirds contained selections from various albums, rather than complete albums. People make such tapes to have more convenient access to their favorites, as well as to take in their car or to the beach. Can anyone doubt that this trend to portable music has helped sell records and tapes?

The other obvious reason for recording from one's own records is to preserve them. It is the real music lover who buys a record, then wants to make a high quality tape of it--of higher quality than he can buy prerecorded--before the inevitable scratches and pops show up.

How about the minority of tapes of prerecorded music not made from one's own records, tapes and discs? Yankelovich found that 21% of the tapes in people's collections were from FM radio. Nowadays, more than ever, FM radio is considered to be a promotional medium. It is very rare that stations play entire albums, and air time for popular singles is eagerly sought. Under these circumstances, recordings from FM can hardly be said to displace album sales. Rather, as I will get to in a minute, they probably promote them.[2]

We don't deny that sometimes people make copies for friends, just as they sometimes pass on a book they've read.

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[2] How record companies will ensure that radio stations play only encoded software is uncertain. Are stations free to play unencoded software? If a premium is charged to stations for the right to play unencoded software, is this tantamount to enactment of a performance royalty?

Does such essentially unremarkable, socially normal behavior warrant intervention? No, because the effect is not necessarily to displace sales. First, someone has to buy the record or tape that is copied. The person who receives the copy would not necessarily have bought that record or tape. In other words, through blank tape people invest more in music, but not necessarily any less in prerecorded music. Moreover, Yankelovich found that after hearing a performance or performer on tape, the taper often will go out and buy the entire record, or another record by the same artist or composer.

The Decoder Chip Provision Would Harm Only the Beneficial Taper

I have engaged in this analysis of taping behavior for two reasons. First, it shows that even when uses that don't involve prerecorded music are not considered, the royalty tax is a penalty on good customers, rather than the solution to any problem. Second, it allows me to demonstrate that the decoder chip provision, if it causes recorder manufacturers to choose between selling recorders with decoder chips or selling higher priced ones without them, has the same problems as the tax itself: it attacks the typical, "good" taper, who seeks quality, portability and convenience, rather than the occasional and, we believe, atypical taper who may, in part, be motivated to save money.

Only the person who is interested in quality will want a new tape recorder, given the fact that he must choose between buying one that is unable to record certain software or one that is much more expensive. The person who wants to be sure he can keep buying records and keep making the highest quality recordings from his own records will pay the extra royalty tax to buy a new recorder without a decoder chip. This is a senseless, insulting imposition.

The reality is that as soon as this provision goes into effect, the typical home taper, who is interested in both quality and buying records, will be forced to pay either an unwarranted tax on his recorder, or an uncontrolled premium on his records, tapes and discs--assuming he can find any - plus a tax on blank tapes.

Now, what about "kids" who allegedly tape only to save money?[3] Since sound quality is not their primary goal, they can continue their practices so long as they have an old recorder handy. And in the unlikely event they have to buy a new one, the decoder chip technology will encourage them to beat the premium on unencoded software. If these are the people who allegedly split the cost of new records several ways, they can split the cost of the royalty tax on a recorder without the chip and purchase the encoded software.

Mr. Chairman, in all seriousness, any provision that requires decoder chips, penalizes people for not having them, or makes recorders without them more expensive is the consumer electronics version of the neutron bomb: it wipes out the people interested in buying music and making quality recordings for their personal use, while it leaves totally unaffected the very few who are said to be creating a "problem" for the recording industry.

Conclusion

Mr. Chairman, in our view the fundamental misperception about home taping is that there is, or will be, any problem that needs a solution. Our Coalition has fought every royalty tax proposal, pointing out the inherent problems of unfairness and overbreadth. Apparently, in moving on to decoder chip ideas, the Subcommittee is looking for a "magic bullet." If this system is one, it is aimed at all the wrong people.

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[3] In fact, the Yankelovich survey found that virtually no one tapes only to save money. Only 1% of those surveyed listed cost as the only reason. Yankelovich survey at 21, 91-93.

The manufacturers who do not wish to adulterate their products, and the retailers who do not wish to sell such products, are sincere in their belief that the hardware and software industries are mutually and equally beneficial. If anything, new technology, recently introduced by the hardware manufacturers, has provided out-of-scale benefits to the software proprietors who are keen enough to take advantage. In baseball, they say that sometimes the best trade is the one you don't make. I respectfully submit that in home recording, the best solution is to leave well enough alone.

Senator **MATHIAS**. Thank you, Mr. Ferris.
Mr. **MANN**.

STATEMENT OF BARRY MANN

Mr. **MANN**. Thank you for inviting me to testify on the Home Audio Recording Act and antiduplicating technology.

I am Barry Mann, and I own and manage David Mann Audio in Philadelphia, PA.

I have reviewed S. 1739, and I have been learning about the antiduplicating technology. Based on what I know about this technology, I do not like it.

Before I talk about the antiduplicating technology, I want to make it clear that I do not think it makes much sense to talk about a solution before there is any agreement there is a problem. I think I speak for thousands of retailers who own record shops and audio stores, and tens of thousands of consumers. And I do not believe that home taping is a problem that needs fixing.

Because my customers and I oppose the notion of a tax in the first place, I think discussions about details of this legislation are premature. I say details about the bill because this discussion of antiduplicating technology is really a discussion about a part of the bill which sets forth exemption. I do not think it accurate, however, to call the antiduping technology an exemption to the audio royalty.

Few of my customers would feel exempted from this legislation when their ability to enjoy the music they buy would be so severely limited. My customers feel they have a right to tape records they buy, and they do not think they should have to pay extra for this right. Why should they not be able to make their own records portable? Why should they not be able to make their own customized tapes from their own records?

I see the potential for major disruptions to my business. This technology puts the absence of a signal on prerecorded music which can be read by a decoder chip. As I understand it, as a practical matter, I would be forced to carry two kinds of prerecorded music. One type to satisfy my customers who want to record, and one type without the signal who do not want to record. This would cause me to have six types of inventory. People who wanted to be able to record would pay more for records without the signal.

This inventory, the dual inventory, would cause two problems. First, the increase in prices for records without the signals would affect sales. Would people, all of a sudden, pay much more for a record that was identical to a record they could have bought before this law was enacted? Of course, they would not want to pay this cost, and sales would suffer.

Consumer reaction to the records with signals will also be very negative since they will feel they are getting a product that lacks a feature, the right to tape, which they already enjoy.

Second, financing and floor space limitations will severely restrict the ability of record merchandisers to double current inventory which is what this technology would require. Doubling inventory would require a lot more space which would greatly increase rent. Even worse would be the effect on financing costs, which are already very high. Even with the interest rates coming down, it is difficult to carry the debt on this inventory. When many of the record companies want capital up front, we have to come up with the cash so we can continue to buy all the new records that are released each week. Failure to have the latest music can cost us our customers. The prospects of carrying each album in six different formats scares me. And it is just not financing costs.

What about the risk I have of not selling my products or of miscalculating how many of each album and in which format I should order. Certainly there would be severe problems in offering adequate selections of classical music.

Unfortunately, many classical works stocked as single titles will be squeezed out. With this new technology, the number of purchasing decisions doubles and the risk of my making a mistake increases accordingly. I think I speak for most retailers when I say the impact could be drastic.

There would also be a dual inventory for hardware if this technology were adopted. Machines with the decoder chips would be exempt from the tax, and machines without would cost more.

I sell hardware and I am concerned about what will happen if this law passes. My guess is that hardware sales would plummet as customers decided to do everything possible to keep their old machines working. Who would want these new machines with the decoder technology?

I am also concerned about record companies getting together as a group to discuss how to price music lacking signals. For instance, if they say as a group the right to tape is worth *x* dollars, for every record without a signal, they would set a standard price hike. Even for the records with signals, they could set prices by saying that such records should cost *x* percent less than a record without the signal. This industry does not have a lot of players among the record producers. I am troubled by anything that allows the big six companies to rigidify prices I can charge for records.

At bottom, I think the whole idea is crazy. It is bad for everyone. I lose, my customers lose, and the whole industry could lose. Introducing this kind of technology at a time when consumers are getting excited again about music is asking for trouble.

I can remember, not too long ago, when my customers were spending billions of dollars of their entertainment money on home computers and video games. Now that I am getting these people back into my store, this technological fix will drive them back out. That kind of fixing this industry does not need. Please leave a healthy industry alone.

[Mr. Mann's submissions for the record follow:]

PREPARED STATEMENT OF BARRY MANN

Thank you for inviting me to testify on the Home Audio Recording Act and the antiduping technology.

I am Barry Mann and I own and manage David Mann Audio Store in Philadelphia, Pennsylvania. I have reviewed S. 1739, and I have been learning about the antiduping technology. Based on what I know about this technology, I don't like it.

Before I talk about the antiduping technology today, I want to make it clear that I don't think it makes much sense to talk about a "solution" before there is any agreement that there is a problem. I think I speak for thousands of retailers who own record shops and audio stores, and tens of thousands of consumers when I say that I don't believe home taping is a problem that needs fixing.

I am in the audio business and I sell prerecorded music for a living. I also sell blank tape. I do not see these sales of blank tape as costing me sales of prerecorded music. In fact, the people who buy the blank tape are my biggest purchasers of music. In speaking to my customers, I have learned that when they buy records they often tape the album to preserve the music. My customers also tape albums because they want to make their music portable, but are dissatisfied with the quality of prerecorded tapes. I don't think these people are stealing from the record companies, and I oppose efforts to make them pay more for the right to tape their records. Because my customers and I oppose the notion of a tax in the first place, I also think discussions about details of this legislation are premature.

I say "details" about the bill because this discussion of antiduping technology is really a discussion about a part of the bill which sets forth "exemptions."[1] I don't think it is accurate, however, to call the antiduping technology an exemption to the audio royalty. Few of my customers would feel "exempted" from this legislation when their ability to enjoy the music they buy would be so severely limited. My customers feel they have a right to tape records they buy and they don't think they should have to pay extra for this right. Why shouldn't they be able to make their own records portable? Why shouldn't they be able to make their own customized tapes from their records?

Why is the government getting involved anyhow? The music industry is doing just fine. Right now my customers are happy. They're buying like they never have before. Record companies are enjoying their best revenues ever. New artists and new acts are constantly entering the business. The compact disc is creating a comeback which is only slowed by the failure of the record companies to make enough discs to satisfy demand. Once this is corrected, the sky's the limit. So why is the government interfering? Decisions about what kinds of machines should be manufactured and what kinds of software I should sell are none of the government's business. You may say that the government is not requiring the use of this technology, but I don't see it happening without legislation making it happen. Because the Home Audio Recording Act provides an exemption for equipment with such technology, the government is basically forcing this idea upon the market. I urge Congress to stay out of the music market.

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1. An "audio recording device". . . . does not include a device . . . (c) which incorporates a decoder or similar mechanism that prevents the device from reproducing, or permits the device to reproduce, the sounds embodied in a phonorecord or copy in accordance with special instructions encoded in the phonorecord or copy for that purpose.

Having made these introductory remarks, let me give you some specific reasons why I, as a retailer, oppose the antiduping technology. I see the potential for major disruptions to my business if the encoder chip technology is adopted. This technology puts a signal on prerecorded music which can be read by a decoder chip added to the hardware. As I understand it, as a practical matter, I would be forced to carry two kinds of prerecorded music. In order to satisfy my customers, for every record, tape, and compact disc without the signal, I would have to carry another record, tape, and compact disc with the signal. People who wanted to be able to tape music would pay more for the records with the signal. I assume adding these signals will cost something and thus even the cheaper records would increase in price over the current price of records.

This dual inventory would cause great problems. First of all, the increase in prices for records without signals would affect sales. Would people all of a sudden pay much more for a record that was identical to a record they could have bought before this law was enacted? Of course, they wouldn't want to pay this cost and sales would suffer. Consumer reaction to the records with signals will also be very negative since they will feel they are getting a product that lacks a feature: the right to tape, which they already enjoy. Again, I and other record sellers will lose sales.

Second, financing and floor space limitations will severely restrict the ability of record merchandisers to double current inventory which is what this technology would require. Where will we put all the additional records, tapes, and discs with these new signals? Doubling inventory will require a lot more space, which will greatly increase rent. Even worse would be the effect on financing costs, which are already very high. Even with interest rates coming down, it is difficult to carry the debt on this inventory. When many of the record companies want capital up front, we have to come up with the cash so we can continue to buy all the new records that are released each week. Failure to have the latest music can cost us our customers. The prospects of carrying each album in six different formats - record with signal, record without signal, cassette with signal, cassette without signal, compact disc with signal, and compact disc without signal - scares me a lot.

And, it's not just financing costs, what about the risk I have of not selling my products or of miscalculating how many of each album and in what format I should order. Already if a retailer buys 12 records, 12 discs, and 12 cassettes of "Born in the USA," he runs the risk of getting stuck with extra records if people decide they want only discs and cassettes. With this new technology, the number of purchasing decisions doubles and the risk of making a mistake increases accordingly. I think I speak for most retailers when I say that the impact could be drastic.

There would also be a dual inventory for hardware if this technology was adopted. Machines with the decoder chips would be exempt from the tax and therefore cheaper; machines without the decoder chips would cost more, but would be able to copy cheaper software. I also sell hardware, and I am concerned about what will happen if this law passes. My guess is that hardware sales would plummet as customers decided to do everything possible to keep their old machines working. Who would want these new machines with the decoder technology anyway?

Third, I am concerned about the record companies getting together as a group to discuss how to price music lacking signals. For instance, what if they say as a group that the right to tape is worth X dollars. For every record without a signal, they would set a standard price hike. Even for the records with signals, they could set prices by saying that such records should cost X% less than a record without a signal. This industry doesn't have a lot of players among the record producers. I am troubled by anything that allows the big six companies to rigidify the prices I can charge for records.

At bottom, I just think this whole idea is crazy. It is bad for everyone. I lose, my customers lose, and the whole industry could lose. Introducing this kind of technology at a time when consumers are getting excited about music again is asking for trouble. I can remember not too long ago when my customers were spending billions of dollars of their entertainment money on video games. Now that I'm getting these people back into the stores, this technological fix will drive them back out. That kind of fixing this industry doesn't need. Please leave a healthy industry alone.

RESPONSES OF BARRY A. MANN
TO WRITTEN QUESTIONS POSED BY SENATOR SPECTER

Specter: What reasons do your customers cite to you for their desire to tape music?

Mann: Because of the very personal, one on one, sales presentations we make at my shop I am in a unique position to find out what it is that customers do with their tape recorders. Before talking about a specific product I interview my customer to find out his or her needs so that I can recommend the best product for the situation. Therefore, as a tool for myself, I classify my customer as an active or passive user of equipment. A passive user, the majority I might add, has an interest in music and the equipment is simply the vehicle to bring the music into his surroundings. An active user, on the other hand, has an intense interest in the equipment and its operation. For the active user, the act of operating the equipment gives great pleasure, easily as much as the music. This observation should not be startling if we just recall the teen with a car, "cruising" on Saturday night. Simply operating the car and "going" is the thing, destination is unimportant. I would like to share with you an informal survey I made before coming to this hearing.

I surveyed my staff and asked, "what is the most often cited reason for buying a tape machine?" The results (given in decreasing order of importance) are:

(1): "I want to record my records for the car."
"I want to record my records for my personal portable."
"I want to record my old records for convenience."
"Most prerecorded cassettes are poor in quality and I want to make my own higher quality tapes."

(2): "I want to save my records from wear."

(3): "I want to make party tapes from my records."
"I want to collect my favorite songs on one tape."

(4): "I want to tape from the radio when I'm not home."

My staff's observations agree with my own. No one mentioned any type of activity which might suggest compromising the rights of the copyright holder. After noting the above responses I asked specifically if my staff felt any copying of unowned records was intended. After some deliberation the staff admitted that such activity probably takes place from time to time but infrequently, mostly to dub out of print, hard to find records or radio and TV one time events. The message was clear. Copyright holders are not at significant risk.

I think it would be useful for me to share with you my analysis of these groups.

The first group is what I call the reformatters. They are merely changing from one form such as an LP or Compact Disc to tape. Many times the musical work is not available on tape at the time the customer wants it. (Record and prerecorded tape purchases are primarily impulse purchases.) Even if the work was originaly on tape, prerecorded tapes usually have only 18 to 25 minutes per side--timings inherited from LPs. By copying the LP or prerecorded tape, the customer can pack two or three complete albums on a 90 minute cassette tape. In a portable context this means less tape to carry around. Clearly this activity is not diverting any revenue from the copyright holders and is simply satisfying unaddressed needs.

The second group is merely making -- and here I will draw a term from the computer industry -- a backup of their music. LPs and tapes are fragile, deteriorate with each playing, and particularly in portable use, are quite often damaged. If a favorite work is damaged after going out of stock at a store or worse, after going out of print, it is lost and the individual is out of luck. Music is not a disposable item.

The third group wants to makeup custom anthologies from their records and tapes. These anthologies could be period or style themes or simply a collection of favorites. In many ways this is a variant of group one, however, group one tends to be passive and records complete sides of LPs without editing while group three, the active user, copies one song at a time.

Group four users are simply time shifters and operate in the same fashion as the video tapers. This activity injures no one.

In summary all four groups, reformat, backup, anthology, and time shift are using their tape recorders in non infringing, "fair use", ways to address needs which, in my opinion, cannot be addressed profitably at reasonable cost to the consumer on a mass or custom basis.

Specter: I understand that your position is that you do not perceive the existence of a "home taping problem" and that you do not want the government to interfere in this business. Can you explain to me exactly what disruptions you would predict to your business if royalty fees and/or encoder chip technology are adopted?

Mann: Basically S.1739 would significantly affect the lifeblood of any retail merchant -- his inventory. Overnight the cost to purchase, own and manage my inventory would skyrocket.

The most obvious impact would be the increased cost of doing business due to the dual inventory of each music format and both types of hardware. There are several facets to the dual inventory problem. There are direct costs of raising the extra capital to finance the doubled inventory and the extra space to house and properly display this inventory, and the extra clerical costs of administering the inventory. There are also numerous indirect, more difficult to define costs. For example indirect costs accumulate for advertising which would then be forced to track which version, encoded or nonencoded, is offered for sale, the costs associated with the confused consumer purchasing the wrong format then wanting an exchange and so on.

The risk of making an unfortunate stocking decision for the retailer also doubles. Not only must the retailer predict which music titles or hardware models to stock, but also predict the encoded/ nonencoded ratio correctly -- or face a double penalty. The record industry's "generous return policy", (allowing me to return unsold inventory for credit) which would allegidly alleviate this problem is not universal at this time. The smaller labels cannot afford it. Even if universal this return policy does not cover my $.20 to $.40 (depending on the size of the operation) per LP cost of packing and shipping these returns. There is also a more subtle inventory problem which shows up after some deeper analysis.

Now, let us look at the life cycle of a product for a moment -- and this cycle holds for all levels of distribution from manufacturing to retail (we not talking about consumables such as food). A new product is introduced with a big promotion announcing its arrival and superiority possibly accompanied by some type of price incentive to get a few into consumer homes. At mid life the product sales and price are stable. Finally technology or fashion moves on and just about everyone who will purchase the LP or model XYZ tape deck has done so and sales drop off to the point that the remaining inventory cannot bring enough profit to support itself and it is sold off, possibly at a loss, to make room for profitable merchandise. The master pricing strategy recognizes this early, mid, end life structure and we arrange the price to show an overall profit for that model cycle. With the dual inventory we would be guaranteed to have more inventory at the end for each model and, accordinglly must raise prices to cover the difference.

One could go on and on with ever deepening analyses. My point is that the dual inventory will raise the cost of doing business significantly, on an ongoing basis, for all concerned -- retail, hardware and software manufacturers -- and ultimately the consumer. This will cause increased costs to the consumer beyond the several hundred million dollars contributed directly by the proposed royalty tax.

Next, let us consider some of the more obvious effects on sales. The increased cost of blank tape to the consumer will decrease my profit on tape sales because the consumer has a relatively fixed budget for tape. This means for the same dollar amount of sales my costs would go up a penny per minute of tape. This would be particularly vexing because competition keeps tape profits very low as it is.

Hardware sales impact is very difficult to predict with much precision because the marketplace is involved. Here we are not just talking about record store "A" competing with record store "B", but record and audio stores competing with other leisure industries for the consumer's discretionary spending. Effectively the royalty tax plus related additional operating expenses, pile a several hundred million dollar per year burdon on my industry. Because of the very price sensitive nature of these purchases, I would be put at a tremendous competitive disadvantage compared to other leisure industries. The consumer will, correctly, perceive himself as being forced to pay more for less. And for yet an additional fee, he will be able to repurchase the privilege, now considered a right, to record. This backward step in price/performance will obviously cost me sales, but worse, it will cost me significant market share which will go to other industries.

With respect to software sales, I assume the record manufactureres, with their share of the royalty tax windfall, could hold the line on pricing -- at least for the encoded version. However the sales pattern will change because of a change in my inventory depth. As a retailer I cannot afford to double my inventory only to stay at the same sales level. That just does not make sense. I can always find room for the fast movers, the superstars. However, the additional, dual shelf space will be taken from the smaller classical and jazz titles which can barely support themselves now on my shelves and certainly could not support their dual version. As a result the small title will be squeezed off my shelves. The argument that the manufacturers, having profits assured by the royalty tax distributions, could then afford to issue the marginal titles is moot. I would not be able to afford to sell them. Therefore, as a practical matter, the small title will not prosper and a fundamental goal of proposed S.1739 will be nullified.

Senator **Mathias**. Thank you, Mr. Mann.

Mr. Ferris, you were here in the room during the demonstration this morning. Could you tell any difference between the coded and unencoded recording?

Mr. **Ferris**. None whatsoever. I have probably a less discerning ear than yours though, Mr. Chairman.

Senator **Mathias**. Well, that would be a contest that I think neither of us would want to enter.

Mr. **Ferris**. But I think, or better, I accept on faith that the chip in that machine technologically works extraordinarily well. But that chip, in my mind, is really a four letter word meaning double taxation.

Senator **Mathias**. Well, before we get to that question, your coalition did have some experts attend a demonstration of this copycoder several weeks ago.

Did they hear any difference?

Mr. **Ferris**. No. I am unaware of any differences that were discerned at all. They were up as observers in the laboratory, and I accept, Mr. Chairman, that the chip works.

Senator **Mathias**. Yes. And I understand that whether it works or does not work does not make any real difference to you. It is the concept and the principle to which you are objecting?

Mr. **Ferris**. Absolutely.

Senator **Mathias**. I thought it was helpful, at least for the record, to establish that you see no technological problems in it.

Mr. **Ferris**. I know of none, Mr. Chairman. And I will accept the record on that, that this technology would work if it has a purpose to perform.

Senator **Mathias**. They say it is cheap, it is durable, it is easy to install, it is hard to defeat, and it is not likely to become obsolete. And you, generally speaking, would stipulate that those things are true. I am not trying to bind you or anything. But I want to be clear: we do not have any real arguments on those points?

Mr. **Ferris**. No, I have no argument that the chip will do what the testimony this morning said it would do. Beyond that, Mr. Chairman, I pass.

Senator **Mathias**. And, of course, it is a prospective solution. It does not do anything about the past or the present really. It looks to the future as a solution to the home taping problem.

Tens of millions of recorders in use today will continue to be able to to copy encoded or unencoded records or tapes or compact discs.

With respect to the equipment royalty, what is your view of the harm that the American consumer would suffer today from the enactment of this legislation?

Mr. **Ferris**. I would first want to get clear from you, Mr. Chairman, who the group is whose behavior we are attempting to alter.

I heard at the last hearing here it was the kids who were making copies and distributing them. And, therefore, there were sales that would be lost.

Is the group we are attempting to reach all home taping? Are we ultimately attempting, when the full technology is in effect, to prevent me from buying source material and making a tape of that for my own personal use? We get wrapped up in the technology, how to get there and even into the hubris of attempting to distribute a royalty in creative ways. But I do not know who it is, Mr. Chairman, whose behavior we are attempting to affect.

Is it mine when I buy a record and make a tape for my own personal use in my own home? Is that to be prevented? I did not hear from the proponents at any time what it was. They slipped back and forth from the kids and the anecdotes to a technology which was fully implemented. And if the software is not made available it will, in effect, under some of the scenarios, prevent all home taping.

Senator MATHIAS. I cannot speak for all the parties to this on either side. So we at least have a common ground to discuss.

As far as I can see, nobody wants to prevent anything. Perhaps Mr. Golodner came closer than anyone this morning to identifying what we are trying not to prevent but to protect: it is the creative contribution of the artists that have made possible the recording in the first place.

Now, Mr. Mann talks about the difficulties that this legislation produced for him. Let me put a question to him that I think puts him in the same position in which Mr. Golodner sees his friends.

If in your store one morning a group of customers came in and simply took records off the shelves and walked out the door without paying, how would you feel about that?

Mr. MANN. Well, I would feel poorly, of course. I do not see how this relates.

Senator MATHIAS. All right. If I can, in order to answer Mr. Ferris' question, suggest that that is what Mr. Golodner sees as happening to his friends. They have produced a product. It is a product made of sound and image rather than of metal or vinyl. But in their minds, and in the eyes of the law, it is still a product. He sees people coming in and taking them off his shelves without paying for them.

That is reducing this problem to its simplest proportion. Now that is where we are. And frankly, we in this committee asked for your help in trying to solve it. I must say that I think it is a problem.

Mr. MANN. I think we disagree on that point.

Before I came down here, I surveyed my staff. We are a very customer service oriented business in my store. And before we sell anything, we ask the consumer: "What are you going to do with this product?" With regard to cassette decks I asked my staff, "What kind of answers do you get?" And the most frequent answer was, "I want to make a tape for my car," and these are all for records that they already own, or "I want a tape for portability."

So they are just changing the format. The formats that possibly are not even available.

The second most popular response was, "I want to protect my LP." LP's are very fragile. And they will purchase the record then, transfer it to tape, and then listen to the tape. If something happens to the tape, they will make a new copy.

That was the end of the reasons. I pressed, and I asked, "Did someone come in and say they wanted to record a record collection?" No one could recall ever getting a response like that.

So I am not sure there is a problem.

Senator MATHIAS. Of course, in the extended hearings that we have had on this subject we have been looking and groping for an answer that would be fair to you as well as to the recording artists. We have looked at the various statistics. If the statistics are accurate, and I have no reason to believe they are not, then some of your customers have a lot of cars. [Laughter.]

Is that not true?

Mr. MANN. I do not see it in my customers. They would have no reason to——

Senator MATHIAS. Well, somebody is buying a lot of blank tapes. If it were confined to just the personal uses that you have described—and I accept the answers that you reported to the committee—then there are just a lot of unexplained blank tapes being sold.

Mr. MANN. They are used for so many purposes.

Senator MATHIAS. I think that is precisely it.

Mr. MANN. Such as—now, are you speaking of all blank tapes and assuming that all blank tapes are going to home taping——

Senator MATHIAS. Well, people are using them for something.

Mr. MANN. I have a lot of friends who use them for computer programs. There is a lot of dictation going on. If you go into a university, you see a lot of people taking notes in their pockets now. That takes a lot of cassettes.

Mr. FERRIS. As a matter of fact, Mr. Chairman, I think the record before this subcommittee demonstrates that a majority of the uses of blank tape have nothing to do with prerecorded music. So we eliminate 50 percent, over 50 percent of all of those purchases of blank tape that have nothing to do with music.

And then we are talking about what the other 50 percent is used for. And I think the studies that are part of the record before these extended hearings demonstrate what the uses are for.

Senator MATHIAS. All right.

Well, now this gets to an argument that you made before, Mr. Ferris, here. You frequently have argued that this approach is too broad. And you have stated in the past that it unfairly harms those who record themselves, let us say, playing a guitar or a class lecture. Let us assume that a student is not willing to listen the first time and wants a second chance so he takes a recorder into a class. Or even a sermon in church. All of these are possible uses for tapes.

But, by this proposal, do we not impose a royalty on machines that are designed to duplicate prerecorded material, and thereby eliminate the overbreadth concern that you have?

Mr. FERRIS. First of all, the breadth is still there. You are imposing a penny a minute tax on all tape which is going to include all of the majority of uses that have nothing to do with prerecorded music. So, overbreadth is still there with respect to the royalty you are collecting on blank tape.

So what I have attempted in asking my question early, Mr. Chairman, was to find out who it is whose behavior we are attempting to modify.

Are we attempting ultimately to eliminate all home taping? I know Mr. Golodner would like a royalty every time we played a record at home.

Senator **Mathias**. But are we not trying to do this? Would you not agree that the bill permits consumers to use the taping machine in noninfringing way?

Mr. **Ferris**. The present machines are noninfringing ways.

Senator **Mathias**. The bill allows the consumers to benefit by purchasing a royalty free machine if it has a decoder. That is right, is it not?

Mr. **Ferris**. What I am saying, Mr. Chairman, is I want to find out whose behavior we are attempting to modify. Where are we attempting to get from this royalty?

Now, on the sale of tapes, you get a royalty from everyone who buys a tape, whether it has anything to do with music. We would like to find out who it is we are focusing on.

I thought at the last hearing it was the kids who were attempting to save money. I do not know who it is now. Is it me when I buy a record and choose to make a tape to preserve that original master copy that I purchased of the artist so that I have that and I can listen to the purity of that recording? Do you want a royalty for that activity?

Senator **Mathias**. Let me put it to you this way.

What about somebody who buys a royalty free machine that has a encoder? What about a royalty free tape?

Mr. **Ferris**. Well, if I buy a royalty free machine, if I buy the royalty free machine which has the chip in it, and if I want to record——

Senator **Mathias**. You can go to church and you can record the sermon, and you can come home and hear it again. It only costs you a nickel.

Mr. **Ferris**. OK. But if I do want a whole tape, if I want to take it home, I have to pay a premium, the premium for which is going to be established by the record companies in some mysterious way, and maybe in some mysterious meeting, not by Congress. Am I to have the right to tape? And your bill, the bill before this committee, says that home taping is not an infringement, but I have to pay a royalty on the software to continue taping.

So, yes, I am paying a tax there. I am paying a royalty tax to be able to tape at home because I bought the machine with that chip. So I have to pay a premium for the software that is going to permit me to tape at home. And I am going to have to pay another royalty tax when I buy the blank tapes. So you are going to hit me with two taxes.

Now your questioning this morning, Mr. Chairman, had great insight into what probably could happen. What would happen? Who is going to control the inventories and the availability of software for that machine I purchased with a chip? All of that software that would permit me to continue home taping in the discretion of the recording companies could be obliterated over time so that I will no longer have a right to tape in the home, which this bill declares is my right if I pay that royalty. That is, unless the Government is going to involve itself in a detail of regulation that since has passed from the Washington scene.

Senator **Mathias**. You are right, all of this would happen in a mysterious way. That mysterious way is known as the free market system. We are trying to set up a system by which market forces will in fact determine how this royalty works.

Mr. FERRIS. Mr. Chairman, what a free market system! You have heard the manufacturers of audio equipment say they would never choose this. You have heard the retailers say that they do not want to sell it, that it will complicate their lives by quadrupling the inventory and thus reduce by a fourth in effect the amount of floor space they have. That is a free market solution?

This is Government meddling into the technology. It is nothing but a technology to collect a tax. And the amount of the tax is going to be determined by the recording industry. And they have already got a marvelous scheme of how to distribute that.

I would like to hear them agree that the distribution methods they described this morning are ones that they will adopt for the present royalties collected. They must demonstrate some credibility. I did not hear them say that they will use these distribution schemes to help today's struggling artists, and thus take from the present wealthy royalty beneficiaries. They are talking about hundreds of million dollars that they hope to collect in the windfall of the proposed legislation.

I can be very creative, too, Mr. Chairman, on how to distribute hundreds of millions of dollars if you will create me a fund. And I can get a great consensus, as well, if it is going to be a windfall for everyone who is going to participate. So I think their credibility on the distribution is something that remains to be established.

Senator MATHIAS. You mentioned software. I am told that Mr. Mann sells an unusual type of software. Is that right, Mr. Mann?

Mr. MANN. Yes.

Senator MATHIAS. What can you explain to the committee about the master copies that you sell?

Mr. MANN. You can think of them as the premium records.

Senator MATHIAS. They are what?

Mr. MANN. They are made on better vinyl than the run of the mill record. You are paying $16 to $18 for them. And people feel that they sound better. That feeling is just about unanimous.

Senator MATHIAS. All right.

Do you make the copies of these masters, or do your customers take them home and make them?

Mr. MANN. They will make a copy—you can think of it as a backup if you are into computers—to protect the original.

Senator MATHIAS. Yes. But where does this happen?

Mr. MANN. It happens in the customer's home, on his own time.

Senator MATHIAS. And what happens to the master?

Mr. MANN. If the customer has a vault, it will be locked in the vault so nothing could happen to it. These records are considered to be treasures.

Senator MATHIAS. But who owns them? Does the customer buy them or do you retain the title to them?

Mr. MANN. Oh, no, the customer buys them. These are—other than the cost and the quality, these are normal products. It is like buying your best china in some respects. You do not use it every day. You bring it out for a special occasion.

This dual inventory, I think, would injure the consumer. Earlier, a drug store example was mentioned where we might have several competing brands of aspirin. My problem is much larger than that. It is not a question of me having 10 faces of each product and I just take one face out of each manufacturer to squeeze down for a new brand. I have thousands of titles that I would now have to duplicate. It takes much more space to do that.

Senator **Mathias**. Let us go back to the master copies for just a minute.

Are these primarily attractive because they can be copied?

Mr. **Mann**. No; they are attractive because they sound better.

Senator **Mathias**. But they also copy better, right?

Mr. **Mann**. Yes; this would be—if you buy a premium camera versus one of the little personal cameras, it will make a better picture. If you then copy it, it will give a better copy.

Senator **Mathias**. Do you sell the albums and their prerecorded tapes that most of us think of when we are talking about this general subject? I mean you have a general brand of merchandise in this area?

Mr. **Mann**. I am a specialist.

Senator **Mathias**. You are a specialist?

Mr. **Mann**. Yes.

Senator **Mathias**. What is the nature of the specialty?

Mr. **Mann**. We have, in our opinion, upscale merchandise.

Senator **Mathias**. Upscale. So you are not really talking about the type of record outlet that most of us are familiar with as we walk down the street?

Mr. **Mann**. I am very familiar with their business also. I choose to do it my way for my own business.

Senator **Mathias**. I am certainly not critical of that. I am just trying to get a picture what kind of business you operate.

Mr. **Mann**. OK.

Senator **Mathias**. Most of the record stores that have been around for more than a few years have had to adapt to some dramatic changes in their marketing practices. Years ago, they sold only records. Now they have to make a space for cassette tapes, and compact discs. Many of them may also stock video cassettes, video discs, or even computer games. All have gotten to be sort of a part of the business these days.

Now, you have pointed out, and I think correctly, that with each new kind of product, the risk for the retailer increases. But a great many retail outlets survive these kinds of risks and have even enjoyed the benefits of the free market system. They have prospered because they have taken a risk and won.

And they won because they have diversified their product line. If they had stuck to the old 33⅓ rpm wax disc, they would not probably be in business today. But they kept branching out and trying new things and, therefore, they have succeeded.

That being the case, why is it that you think the need to stock encoded records, tapes, and discs will be a pitfall? Doesn't the recording market of the last 25 or 30 years suggests that new products have in fact turned out to be a rather good deal?

Mr. **Mann**. Each of these things that you have cited represents a new opportunity. It was new, improved technology.

The vinyl LP was a tremendous improvement over the then shellac 78's. And then we got into stereo, and there was a short period of time when there was a dual inventory there. But it was clear we were headed in a direction of improved performance and this was a tremendous opportunity.

We are getting into this in compact discs now. There is a tremendous opportunity in compact discs because of the improved technology. To now force dual inventories in all of these categories, and it will not result in any increased sales surely, because we have the same merchandise and now we have to figure out whether the people would want encoded or not encoded media. So we have a burden of keeping track of two sets of inventory for the same sale, for the same title. And we are talking about thousands of titles, particularly the larger record stores, not just a few things.

For example there is an opportunity now that I think is being held back by the inventory problem. I hate to be too technical. Have you heard of the Dolby system, are you familiar with that? [Senator Mathias nods affirmative.]

OK. There is now an improved Dolby, the Dolby-C. I am not seeing any Dolby-C prerecorded tapes on the market, which are a significant improvement over the Dolby-B tapes. It is just too difficult to carry the inventory because you would be forced to have two inventories of cassettes, one with the Dolby-C and one without.

Senator MATHIAS. But is not that the mysterious force of the market? Isn't it that the cost of doing it and the difficulty of doing it does not justify what you would have to charge the customers?

If, in fact, the customers wanted it and were willing to pay for it, you would carry it, would you not?

Mr. MANN. Customers want it and are willing to pay for it. I cannot get it because I would have to collaborate with the manufacturers who have the manufacturing facilities. I think it would be too difficult for manufacturers to deal with the dual inventories of cassettes.

And if Dolby-C tapes were to come on the market with the antiduplicaling technology, we would then have encoded and unencoded versions.

Senator MATHIAS. Let me go back to Mr. Ferris because I interrupted him when he was starting to talk about the distribution plan.

You remember that in our October hearing on this bill, Carol Tucker Foreman stated that she did not think anything in the bill ensured that the royalties would ultimately end up in the pocket of the artist. She said at that time, "You write a bill that says there is absolute security that a starving artist is going to get money and I will pay the tab."

I am not sure that you can speak for her, but how do you think she would feel about the royalty distribution plans?

Mr. FERRIS. I think that was a statement of personal generosity on the part of Carol Foreman, and I do not think it was a government-imposed tax that she was talking about. I commend Carol for it.

Senator MATHIAS. Do you think she would feel better about the proposal before us today than the one that was before us at that time?

Mr. **Ferris**. No, I do not think so, Mr. Chairman, because I think Carol would have as much difficulty in reaching the question of assessing a tax, let alone the distribution mechanism.

This is a marvelous technological solution in search of a problem. And there is no problem with home taping, none that has been defined. It is a moving target. Last time, it was those that wanted to tape to save money, the so-called anecdotal kids. I do not know who it is now.

But this legislation is overbroad because it is going to eliminate capabilities which are presently available, and which are presently legal under the copyright law.

Senator **Mathias**. You may also recall that at the time of the hearing last fall, we submitted some questions to you. We were concerned about the fact that the recording industry asserted that the equipment manufacturers refused to discuss the issue. In response to a question on that subject, you said that while the ARRC has never been approached with such a proposal, you would not be interested.

As we discussed a minute ago, this new technology has been demonstrated to some experts that were selected by your coalition. I wonder if that has changed your position?

Mr. **Ferris**. Not at all, Mr. Chairman.

As you know, our coalition is comprised of not only manufacturers of hardware and not only retailers that sell them, but also a myriad of consumer groups that represent hundreds of thousands and millions of people who are into the music scene.

I think that any effort by manufacturers of hardware and people who create software to enter into a form of arrangement that is going to, in effect, elevate the prices on consumers without justification is one that a manufacturer should have great reluctance to do. Our coalition, which represents consumers, would be breaching our trust for that element of our coalition—the consuming public.

Senator **Mathias**. I assure you that this committee and the Congress at large would not be prepared to see prices raised for consumers without justification. We would object violently to it and would prevent it. And I think we have the power to prevent it.

But we still have the problem which Mr. Golodner stated with a great deal of passion this morning: that there are artists who feel that their products are being taken without compensation.

As an illustration of the existing gulf here, Mr. Mann says he does not see that as a problem. Mr. Golodner sees it as a very big problem.

The best analogy that we could have is to convert Mr. Mann's record store into a book store. In the printing industry there is a pretty clear understanding that for every book that is sold, the author gets a royalty—12 cents, 15 cents, 20 cents, whatever the royalty may be agreed on in his contract with his publisher. If the book is not sold, the author does not get the royalty. But if the book is sold, then the author gets the royalty.

Now, if Mr. Mann's cozy book store sells a book to a customer, who takes it home and runs it through a Xerox machine, it is pretty clear that the author has lost a royalty. Is that not true, Mr. Mann?

Mr. MANN. Yes, he would. We do not know the purpose for that copy. It may be some sort of working copy for the person's own use. Sometimes as a learning experience, you will want to——

Senator MATHIAS. Let me take our hypothetical case one step further.

Your customer at Mann's Cozy Book Store is a labor organizer. And he is buying the book for the purpose of holding an organizational meeting of some kind, and he takes it home and makes 100 copies to distribute to the people who are coming to this meeting.

In that case, the author would clearly have lost 100 royalties that he was entitled to because his creation is going to be employed by this labor organizer to transmit his thoughts and his ideas to 100 people who are coming to a meeting. And he is not going to get rewarded for that use of his intellectual creation, is he?

Mr. MANN. No; In that example—now, are you suggesting that this is what is going on? I do not feel that it is the case in audio technology.

Senator MATHIAS. So your problem is a factual problem. If I could tell you that a recording is being made of a musical creation—which is intellectual property just the same as the printed word represents intellectual property—and 100 copies were made of that recording, and they were being used for some business purpose, you might feel differently about it.

Mr. MANN. There is another aspect to the anti——

Senator MATHIAS. Would you feel differently if that were the case?

Mr. MANN. How many people are each running off 100 copies?

Senator MATHIAS. I am saying the one customer comes in, buys a tape, and for a business or commercial purpose, makes 100 copies.

Mr. MANN. I think there is grounds for prosecuting that person. That is different than a home individual, I think.

Senator MATHIAS. Now we are coming close to the problem.

How are you ever going to prosecute that person? All of this takes place under very private circumstances. What are the chances of ever detecting it? We are talking about the struggling artist, not the superstar. As a practical matter, how is that struggling artist ever going to bring a case? It is just not likely to happen.

Congress is concerned about how to protect the creation of that struggling artist who has been robbed, if you want to use that verb, of a hundred royalties. In this case, unauthorized copies of this work were made and used commercially or in some business way. We are not talking about the car; we are not talking about taking it to the upstairs machine; we are talking about a hundred copies used for business in this hypothetical example.

Now, that is a problem, is it not?

Mr. FERRIS. Mr. Mann's instinct is very good from the standpoint of the copyright law. Because when you are talking about commercial gain, or value, there is a great distinction between what we are talking about here, Mr. Chairman.

We are talking here about recording for personal use, not commercial use.

Senator MATHIAS. But the other cases also exist.

Mr. **Ferris**. If we go to the publishing industry, are they in separate hearings that I do not know about complaining about this issue and pressing legislation? Do they feel that it is a significant problem?

Senator **Mathias**. Yes, they feel it is a very significant problem. That is why this committee has a problem, because they come to us and they say this is a significant problem. They tell us that there are royalties earned by these creative artists which are not being collected, and thus unfairly denied to the artist because of unauthorized recording for unauthorized uses.

We are groping for some means to protect the right of copyright which, otherwise, will become meaningless and which will have an adverse impact on your end of the business some day if we do not find a way of making intellectual property a recognized and protected form of property like any other. Achieving this was possible until the new technologies began to erode copyright.

We are not persecuting the retailer. We are trying to find a way to protect a major industry in America which is showing signs of being a little ragged around the edges.

Mr. **Mann**. I think another person will lose with this antiduplicating technology. About 30 percent of the people who would buy stereo equipment and the recorders are hobbyists. This is an activity that they want to pursue, the act of taping, the act of taking pictures. It is a leisure time activity for them. If they are prevented by this technology of doing that, I think they will suffer a loss.

Senator **Mathias**. We are in a situation where we have evidence before this committee that other people are suffering a loss now. We do not want to impose a loss upon you and your friends. We are trying to find a way to address the loss that the other people are suffering or say they are suffering, without imposing too heavy a burden on you. That is why we come to Mr. Ferris and say will you sit down and address the nature of this problem?

Let me turn to Mr. Ferris because he argues that the encoder would hurt the sales of audio recording devices. I think you said that.

Isn't it the case that once people pay the royalty there would be no limit on the number of copies they could make, even under the hypothetical case that I gave Mr. Mann? The utility of the machine would not diminish. We would simply legalize the practice and make it a proper and a fair thing to do because we would have compensated the parties who would otherwise be injured. So whether taping is a leisure time activity or otherwise, we are making it a perfectly legal authorized practice.

Mr. **Ferris**. Under your framework then, Mr. Chairman, the anecdotal kids, all those who want to save money, could make all the copies they want and give them out as widely as possible.

Senator **Mathias**. Once the royalties were paid.

Mr. **Ferris**. But is that the group that we are attempting to inhibit?

Senator **Mathias**. Of course we would still prohibit taping for commercial gain.

Mr. **Ferris**. That is right. That has always been true.

Senator **Mathias**. That is right. We would still prohibit taping for commercial gain.

Mr. **Ferris**. And that has always been a violation of the copyright law. It is today.

Senator **Mathias**. I think at the last hearing—I may have misapprehended the mood—but I thought there was a general agreement that the people involved in recording and producing records were injured in some degree by home taping, that is, taping for personal, not commercial use.

Mr. **Ferris**. That they were injured——

Senator **Mathias**. Yes.

Mr. **Ferris** [continuing]. In the sense of lost sales?

Senator **Mathias**. Yes.

Mr. **Ferris**. And my question really is——

Senator **Mathias**. They are harmed even in Mr. Mann's example of a fellow who makes a tape to put in his automobile. As innocent as that may be, that is at least costing Mr. Mann a sale. If that were not technically possible, that man would come in and buy two tapes from Mr. Mann. Now he only buys one. So somebody loses something under any kind of home taping. In this case, Mr. Mann loses something.

Mr. **Ferris**. That really is a premise that should be discussed in much greater detail, Mr. Chairman. I think there is much benefit to the recording industry and the artists from the hardware that has been produced that enables music to be heard in all the formats that it is presently being heard.

The record before this committee demonstrates that the recording industry—and I am not an expert on it—has had marketing myopia. They had it when the Walkman came out. Less than half of the titles in their catalogs were put out on prerecorded cassettes, and when they did put them out on prerecorded cassettes, they were on of the most inferior of tape. Those that really wanted to listen to music had to make their own. They could not buy it from the recording industry. And now what is happening with the compact disc, another blossoming revenue stream of the recording industry and the artists? They again have not adjusted to it. You cannot buy compact discs. Their sales have gone up 239 percent in the past year, and you still cannot get them. They have not adjusted at all.

This portability and the ease with which people can hear music where they want to has been a boon to the recording artists and to the recording industry because it has developed revenue streams to them that they otherwise never would have had.

So you should not look at this as lost sales, because if I want to listen to the music I buy in Barry Mann's store at the beach or in my car or when I jog, or if I want to customize to be able to put 90 minutes of my favorites on a particular tape so I can really enjoy them, that puts me more into the music scene. That makes me buy more music.

To want to retard that dynamic, which is what the recording industry is unwittingly attempting to do with this legislation, is to me another example of the myopia that they have had in adjusting to a dynamic scene. Mr. Chairman, the whole notion of lost sales, that I will buy two, or I will buy four, because my kids have cars, is the type of trench thinking that is not new in the whole music industry.

Senator **Mathias**. Now we have lifted beyond that thinking, and we have a technology which permits you to make the tapes for the car and the tapes for the kids, the tapes for the upstairs machine. There it is right at the table beside you.

Mr. **Ferris**. It is the one that I have at home without that chip. It does it now, and it is legal. It is lawful.

Senator **Mathias**. But with the chip it prevents the injury.

Mr. **Ferris**. But I question where the injury is, Mr. Chairman. I do not see the injury.

I think the sales are going wild in the record industry. Why did it have its record year in 1984 and why did it exceed its record year of all time in 1985? If that is injury, it is the type of injury many businessmen in this country would like to have.

Senator **Mathias**. If you recall the October testimony, there is some dispute about that subject also.

I regret that we have to end this hearing with such a wide gap in perceptions. But I am afraid that is the case. You just heard the bell ring for a rollcall vote in the Senate, so I think we have gone about as far as we can probably go this morning.

In spite of the continuing differences in view, I think the testimony today has been useful. I think it shed some light on a limitation on the proposal contained in Senate bill 1739. It demonstrated that it is at least technologically feasible—and Mr. Ferris agrees with that—to manufacture recording equipment that is exempt from the royalty without sacrificing sound quality.

It has brought to light a proposal of a way to structure the royalty distribution system that is worth some thought. It offers an incentive to create, which, of course, is the goal of the copyright system.

As Dr. Johnson remarked, only a blockhead would write except for money. Some reward is supposed to be at the end of the creative road. The royalty distribution proposal attempts to target that incentive. It is a contribution to this debate. There is a good deal of new information as well as old arguments to digest as a result of this morning's hearing.

I suggest that we hold the record open for 4 weeks to give those witnesses who have written questions time to submit their answers. It will provide time for further thoughts and comments from witnesses, and for responses to written questions that may be forthcoming from other members of the subcommittee.

At the end of 4 weeks, we will close the record, and we will then turn our attention to the question of taking further action on S. 1739.

I thank you all for attending. Thanks very much.

[Whereupon, at 12:08 p.m., the subcommittee adjourned, subject to the call of the Chair.]

HOME AUDIO RECORDING ACT

MONDAY, AUGUST 4, 1986

U.S. Senate,
Committee on the Judiciary,
Washington, DC.

The committee met, pursuant to notice, at 10:33 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Strom Thurmond (chairman of the committee) presiding.

Also present: Senators Mathias, Grassley, Heflin, DeConcini, Denton, and Simon.

Staff present: Diana L. Waterman, general counsel; Cynthia Blackburn, counsel; and Laurie Westley, minority counsel.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The Chairman. The committee will come to order.

I am pleased to welcome everyone to the Senate Judiciary Committee hearing today on S. 1739, the Home Audio Recording Act. Under this bill, copyright owners would be compensated for profits which they claim were lost as a result of home taping.

The bill was referred to the Patents, Copyrights and Trademarks Subcommittee, which has held two hearings on this issue. The subcommittee approved this bill on May 21, 1986. This hearing is being held in response to numerous requests to provide further opportunity to express a variety of views on this legislation. I am most pleased that Commissioner Quigg from the Patent and Trademark Office is here to testify on behalf of the administration.

As introduced, this bill proposes to place a royalty on blank tapes as well as taping equipment. I was concerned that the tax on the blank tapes would have a negative impact on those consumers who purchase blank tapes with no intention of using them to record copyrighted music.

At its markup, the subcommittee deleted the blank tape royalty, but kept the royalty on recording equipment. The subcommittee also added a specific formula for distributing the royalties that are collected.

The removal of the royalty on blank tapes is a positive improvement. However, I still have some reservations about the bill. While I am sympathetic to the position that copyright owners are advancing, I am also concerned about the negative effects this bill may have on other segments of the public, such as consumers and retailers.

In this hearing today, we will focus on the bill, as approved by the subcommittee, and the effects it may have on consumers, retailers, and songwriters. I look forward to hearing the testimony today and I thank each one of you for taking the time to present your views.

Now, our first witness today is Hon. Donald J. Quigg, Assistant Secretary and Commissioner of Patents and Trademarks. Now, we would like for Mr. Quigg to present his testimony in 5 minutes and put the rest in the record; the same thing applies to the other witnesses. We have a large number of witnesses and the defense bill is coming up in the Senate at 12. That way, we will have the entire record before us.

Mr. Quigg, we are glad to have you with us and you may now proceed for 5 minutes.

STATEMENT OF DONALD J. QUIGG, ASSISTANT SECRETARY AND COMMISSIONER OF PATENTS AND TRADEMARKS

Mr. QUIGG. Thank you, Mr. Chairman, Mr. Grassley. I appreciate the honor to appear before you today to discuss S. 1739 and some problems which we visualize as being associated with it.

The private copying of copyrighted works has been one of the most important and one of the most difficult issues facing copyright policymakers. The availability of home audio recording devices permitting consumers to duplicate copyrighted works has really compounded the problem.

Making these recordings at very little cost without the permission of the copyright owner or the payment of a royalty is really the source of the problem. Advances in technology will serve to further encourage home copying. Digital audio tape recorders, expected to be introduced within 18 months, will provide home copiers with a perfect master and a copying medium that will permit duplication of perfect copies in a smaller, more convenient cassette. This can be expected to provide greater incentives to home copiers, with a corresponding adverse impact on copyright owners.

In 1980, a CBS market research study indicated that home taping cost the prerecorded music industry from $700 to $800 million annually. A recent Audits and surveys study found that the equivalent of 564 million albums were taped annually.

Based upon those figures and other industry estimates, Dr. Alan Greenspan estimates that home copying cost the recording industry more than $1.4 billion in 1982.

A technological solution developed by CBS Laboratories would prevent unauthorized copying by encoding recordings, by removing a notch from certain frequencies. A decoding device would be built into a recorder's circuitry so that removing it would be expensive and difficult.

This system prevents the copying of tapes with a frequency notch, but tapes without the encoding will be copyable.

The recording industry has stated that the system would be made available royalty-free to any recorder manufacturer. Assuming this technology could not easily be bypassed, unauthorized home copying would be prevented and compensation could be received from those who wish to copy, based on sales of copyable recordings.

Recording companies could set a higher price for copyable records based upon the expected higher value that consumers would be willing to pay for such recordings. Consumers who did not wish to copy could purchase lower-cost encoded recordings that would be playable, but not copyable, on encoder-equipped recorders.

This approach fosters market determinations of royalty levels and distribution patterns. It avoids the use of the Copyright Royalty Tribunal and the necessary regulatory decisions as to the appropriate level of royalties and the decisions as to the parties and respective shares of distributing the fees.

Rather, copyright holders would be compensated according to the sales of copyable records, and artists could be expected to negotiate for their respective shares of that compensation.

Rather than supporting S. 1739, the administration is interested in working with Congress to solve the problem of uncompensated home audio copying through mandatory use of the CBS decoder system. We believe that this is the best approach in solving the problem.

While there are some questions about the specific CBS decoder system, the Department of Commerce is ready to work with Congress to resolve these remaining questions and effectively solve the problem.

There are a number of points in favor of this approach. First, it minimizes administrative costs and permits the market to set the price for the right to make home copies.

It avoids adding yet another compulsory license to the copyright law.

It avoids complexity and governmental involvement in regulation and ratesetting inherent in systems requiring royalties on machines or blank recording media. It permits copyright owners to secure compensation by placing a premium on copyable records.

It eliminates the involvement of the Copyright Office and the Copyright Royalty Tribunal in the collection and distribution of user fees, as this would be left to the free market.

The proposal would avoid imposing additional costs on noninfringing users. The cost of the chip, estimated to be $1 to $5, is an insignificant amount relative to the cost of the recording equipment and the size of the problem.

It responds to the challenge posed by the emerging digital audio tape recorders. It is consistent with administration efforts to encourage strong protection of intellectual property, and sets an example for other nations, especially Third World, to follow.

We look forward to working with the Congress to resolve outstanding questions and develop a fair and effective solution to this problem.

This concludes my prepared statement and I will be happy to respond to any questions you may have.

The CHAIRMAN. The distinguished Senator from Iowa has to leave in just a few minutes. Did you have an opening statement, Senator, or any questions?

Senator GRASSLEY. Mr. Chairman, I do not have an opening statement, but I did want to explain my interest in this issue. I have heard from a number of people in my State about S. 1739 on both sides of the issue.

I have to leave to preside over the Senate from 11 to 12, therefore I will not be able to stay, but I may have some questions to submit in writing. I thank you very much for letting me express my interest.

The CHAIRMAN. If you will prepare your questions and get them to the staff, they will get them to the witnesses.

Senator GRASSLEY. Thank you.

The CHAIRMAN. Mr. Quigg, currently some people tape records or tapes that they have purchased in order to have an extra copy for their car or Walkman. As a matter of policy, is this the type of behavior we should try to prevent, or should this be considered a fair use?

Mr. QUIGG. Mr. Chairman, it seems to me that we have to balance the problem against the solution, and if it is necessary that the individuals purchase an extra copy of a tape in order to use it in their car or home, I thnk that, on balance, it is better to have a simple, easy-to-administer law that applies to copying.

The CHAIRMAN. Now, just in simple words, what do you feel is reasonable and fair to both sides? After all, we want to be fair to both sides.

Mr. QUIGG. Yes, sir; that is exactly what we are striving to do. If we followed the approach which the administration is recommending, there would be a fairly large number of tapes which the recording industry will not see fit to encode.

The CHAIRMAN. See fit to what?

Mr. QUIGG. They will not put an encoding in the tape. In other words, if the tape does not have the encoding incorporated in it, the device can copy those tapes with no difficulty whatever.

It is only those tapes which are apparently valuable enough to justify putting the encoding in them that would not be copyable by the decoder-incorporated machine. And I think that this does give us a balance which is reasonable and just.

The CHAIRMAN. Now, Commissioner Quigg, some suggest that the Congress should drop the home taping issue and concentrate on preventing the large-scale counterfeiting of tapes that is occurring.

What is your opinion?

Mr. QUIGG. Well, Mr. Chairman, I think that both of those issues are tremendously important issues, and I think that the home copying is an issue which the Congress should address, but I do not detract one iota from the importance of the counterfeiting and our need to solve that problem, also.

The CHAIRMAN. Well, if you have any more recommendations in either line, I wish you would get those to us.

Mr. QUIGG. Thank you.

The CHAIRMAN. The distinguished Senator from Alabama.

Senator HEFLIN. I am sorry, Mr. Chairman. I just arrived. I do not have any opening statement and I did not get to listen to this witness and I will defer any questions right now.

The CHAIRMAN. The distinguished Senator from Iowa.

Senator GRASSLEY. I have no questions.

The CHAIRMAN. Thank you very much, Mr. Quigg.

Mr. QUIGG. Thank you.

[The prepared statement follows:]

STATEMENT OF DONALD J. QUIGG
ASSISTANT SECRETARY AND
COMMISSIONER OF PATENTS AND TRADEMARKS
ON S. 1739

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to appear before you today to discuss the problems which S. 1739, the "Home Audio Recording Act," seeks to solve and some of the problems to which it also gives rise. This bill clearly establishes the right of the public to tape musical and sound recordings at home for their own pleasure and amusement without incurring liability for copyright infringement, places a royalty on the means used to make these copies, encourages the use of the new decoder system, and provides procedures for distributing royalties to copyright owners.

BACKGROUND

Ever since the day the Constitution first empowered Congress to promote the "progress of Science and the useful Arts," our laws have sought to achieve the delicate balance between the need to ensure an adequate reward to artists for the enjoyment by others of their creations and the right of the public to enjoy them.

The ultimate goal, of course, is to ensure that Americans have available to them the quantity and quality of works that the intellectual property system was designed to give us.

Today, however, developments in technology as well as the ability of entrepreneurs to identify new needs and to develop new markets pose a constant - and healthy - challenge to that balance. We are continually called upon to examine intellectual property concepts in light of these changing developments. In my view, an intellectual property system that (a) induces a songwriter to compose something that people want to hear, (b) induces an inventor to develop a machine that makes it easier for them to hear it and (c) forces us to take a fresh look at the relevant statutes, is doing the job the framers of the Constitution intended two centuries ago.

That, of course, brings us to the problem that faces us today. Before the development of modern audio recording devices, if you wanted access to a recorded song, you bought the record. The author's exclusive right to reproduce his or her work that lies at the heart of intellectual property law was unassailed in principle and unassailable technologically. That is simply no longer so.

The private copying of copyrighted works has been one of the most important and one of the most difficult issues facing copyright policy makers. Advances in audio recording devices permit consumers to duplicate, at very little cost, recordings without the permission of, or payment of a royalty to, the copyright owner. The expected introduction of digital audio tape recorders will make these problems more acute. To meet the challenges of changing technology, we must devise an equitable and workable system for compensating creators of intellectual property that minimizes Government involvement without impairing public access to both music and the fruits of technological advances.

There have been significant advances in technology which will serve to further encourage home copying. Digital audio tape recorders, expected to be introduced within 18 months, will provide home copiers with a perfect master and a copying medium that will permit duplication of perfect copies in a smaller, more convenient cassette. This can only be expected to provide greater incentives to home copiers, with a corresponding adverse impact on copyright owners.

ECONOMIC HARM CAUSED BY UNAUTHORIZED TAPING

Some private copying of copyrighted works by individuals might fall within fair use, a doctrine originally intended to permit use of portions of copyrighted works for scholarship and research. This doctrine has been stretched to include such diverse concepts as photocopying of journal articles in Williams and Wilkins v. U.S., and off-the-air home video taping (for time-shifting purposes only) of broadcast television programming in Sony v. Universal Studios. Unlike the facts in the Sony case, home audio taping is usually done for the purpose of retaining a copy to build a library.

Without such copying, home libraries would be built with purchased, authorized copies. In 1980, the Market Research Study by CBS records indicated that home taping cost the prerecorded music industry $700 to $800 million annually. A recent Audits and Surveys study found that the equivalent of 564 million albums were taped annually. Based upon those figures and other industry estimates, Dr. Alan Greenspan estimates that home copying cost the recording industry more than $1.4 billion in 1982. The net commercial effect of this copying should preclude the application of fair use to home audio recording.

POSSIBLE APPROACHES TO SOLVE THE PROBLEM

A technological solution developed by CBS Laboratories would prevent unauthorized copying by encoding recordings by removing a "notch" from certain frequencies. A decoding device would be built into a recorder's bias oscillator, as an essential component of the electronic circuitry, so that removing it would be expensive and difficult. When the decoder detects a "notch," it turns off the sound recording capacity of the system for several seconds. The recording industry has stated that the CBS Laboratories-developed system would be made available royalty-free to any recorder manufacturer. The system requires only that a decoder be able to pick up and recognize the frequency notch and disable the recording capability of the recorder accordingly. The CBS system can be used with all digital and analog recording media. It will prevent the copying of tapes with the frequency notch, but tapes without the encoding will be copyable.

CURRENT LEGISLATIVE PROPOSAL

The current legislative proposal in S. 1739, would set up a complex regulatory system to solve this problem. It would involve:

- Payment of royalties on certain tape recorders that do not contain a decoder -- 5% of the first wholesale price for single drive recorders and 25% for dual-drive recorders. Recorders with a decoder element would be exempt.

- Fees would be paid into the Copyright Office for deposit with the Treasury in an interest bearing account for subsequent distribution by the Copyright Royalty Tribunal (CRT) according to a complicated formula including a distribution of statutorily set royalties to artists whose works are likely to be copied, with two percent going to the National Endowment for the Arts for the benefit of artists who have not yet had their works recorded.

- Recorders with only microphone input, play-only devices without a recording capacity, and multiple drive recorders for legitimate commercial purposes would be exempt from any requirement to pay a royalty.

- A system under which certain non-infringing users could obtain exemptions from the payment of royalties.

- No royalty on blank tapes or other audio recording media.

ANALYSIS OF THE ISSUE

Based on the available information, there appear to be no absolute answers to many of the legal, economic and technological issues raised by S. 1739 and the CBS decoder system. Both proponents and opponents of S. 1739 agree that home copying of audio recordings is widespread, but they do not agree upon the consequences of this copying. Opponents argue that home audiotaping stimulates sales of recordings. Proponents argue that the net effect is a substantial loss of sales. On the technology side, both sides appear to agree that the decoder technology would be applicable to all presently available media and devices. The cost of including the decoder technology in recorders is estimated at between $1.00 and $5.00 per unit. Neither side claims that the decoder technology would be easily bypassed.

The Administration believes that, while compensation should be afforded for unauthorized copying, S. 1739 does not provide the best available approach to solving the problem of home taping. First, the statutorily established royalty levels are arbitrary and do not attempt to approximate the market value consumers place on the ability to make copies of recorded works and the amount of copies they would make. Under the proposed five percent fee based on the cost of the recorder, most consumers could be expected to purchase recorders without the decoder element, paying a modest one-time royalty (i.e., $10 on a $200 machine) for the privilege of unlimited copying of encoded records and tapes. This result would undermine the potential use of the decoder technology as a means of permitting copyright owners to achieve royalties directly from copiers, and would ultimately be borne by most consumers regardless of the amount of taping that they do. Second, the statutorily established collection of royalties and formula for distribution of those payments is a heavy regulatory burden, is arbitrary, and does not attempt to approximate the compensation that copyright holders would receive if they were able to charge for the copying of their works. A preferred solution would be to prohibit the manufacture, sale, or importation of new machines without a decoder element. This could result in a situation where the royalties are paid by those doing the copying and only in those instances when they choose to copy.

Assuming this new technology could not easily be bypassed, unauthorized home taping would be prevented and compensation could be received from those who wish to copy based on sales of copyable recordings at presumably higher prices than those charged for noncopyable records. Under this approach, recording companies would be in a position to set a higher price for copyable records based upon the expected higher value consumers would be willing to pay for such recordings. Consumers who did not wish to copy could purchase lower-cost, encoded records and tapes, that would be playable (but not copyable) on the encoded recorders as well as on existing equipment. This approach fosters market determinations of royalty levels and distribution patterns. It avoids the use of the CRT and the necessary regulatory decisions as to the appropriate level of the royalties and the decisions as to the parties and respective shares of distributing the fees. Rather, copyright holders would be compensated according to the sales of copyable records, and artists could be expected to negotiate for their respective shares of that compensation.

Some have argued that such an approach may:

. Encourage use of existing recorders and their repair if consumers defer purchase of new machines with the decoder;

. Encourage development of new technology that would make obsolete existing recorders earlier than might otherwise occur;

. Increase the cost of recorders;

. Encourage expenditure to engineer around the decoder;

. Impose substantial administration and enforcement costs on society including regulation of the placement of the chip in recorders and policing illicit imports, manufacture, and sales; and

. Be viewed as a non-tariff trade barrier.

We believe, however, that these arguments must be evaluated in the larger context of the economic importance of a strong, efficiently functioning intellectual property system to U.S. creators and entrepreneurs and a market approach to the solution of the problem of unauthorized copying.

. The decoder approach will not retard new technology; it depends on a performance standard, not a hardware standard, and it is adaptable to new technology.

. Continued improvements in recorder technology, especially the advent of digital audio tape, will continue to create a demand for new recorders.

- Adding the decoder element to new recorders may add from $1 to $5 to the cost of a new recorder, an insignificant cost for most purchasers.

- Any technology used to safeguard property imposes a cost of engineering around the protection. However, the effectiveness of any technological protection for property is to make the cost of violating the safeguard exceed the benefit of taking the protected property. Neither side asserts that the decoder system would be easy to circumvent.

- The administrative costs of policing the required use of the decoder technology would be small. Performance standards could be established through existing domestic and international private voluntary standards organizations. Other enforcement costs would be borne by the private firms enforcing their rights in the courts.

- It is generally accepted that the copyright law does not provide any blanket exemption for home copying of sound recordings, either directly or through the fair use doctrine. Adopting this solution would only underscore that conclusion and support the Administration's objective to improve the protection of intellectual property at home and abroad.

- As long as the requirement for the use of a decoder applies to both imported and domestic equipment, there is no substance to the trade barrier argument.

There are some areas of uncertainty regarding the specifics of the technological approach.

- How effective is the CBS decoder system?

- Are the CBS system and standards applicable to all present and reasonably foreseeable recording technology?

- How easy is it to bypass the decoder?

ADMINISTRATION POSITION

The evidence appears overwhelmingly to lead to the conclusion that home audio taping has some adverse effects on the recording industry. It is also undisputed that releases of new records are down. Whether these factors are undermining economic incentives to invest money and effort in the production of new sound recordings is disputed by the parties.

In light of our concerns discussed earlier, the Administration would oppose S. 1739 as presently drafted. However, we are interested in working with Congress to solve the problem of uncompensated home audio copying through mandatory use of the CBS decoder system. We believe that this is the best approach for solving the problem. While there are some questions about the specific CBS decoder system, the Department of Commerce is ready to work with the Congress to resolve these remaining questions and effectively solve the problem.

There are a number of points in favor of this approach:

- It minimizes administrative costs and permits the market to set the price for the right to make home copies.
- It avoids adding yet another compulsory license to the copyright law.
- It avoids the complexity and governmental involvement in regulation and rate-setting inherent in systems requiring royalties on machines or blank recording media.
- It permits copyright owners to secure compensation by placing a premium on copyable records.
- It eliminates the involvement of the Copyright Office and the Copyright Royalty Tribunal in the collection and distribution of user fees as this would be left to the free market.

- The proposal would avoid imposing additional costs on non-infringing users.

- The cost of the chip ($1-$5) is an insignificant amount relative to the cost of the recording equipment and the size of the problem.

- It responds to the challenge posed by the emerging digital audio tape recorders.

- It is consistent with Administration efforts to encourage strong protection of intellectual property and sets an example for other nations, especially third world, to follow.

We look forward to working with the Congress to resolve outstanding questions and develop a fair and effective solution to this problem.

This concludes my prepared statement. I shall be happy to respond to any questions you may have.

The CHAIRMAN. Now, we have a panel: Mr. Charles Ferris and Mr. Stanley Gortikov.

Mr. Ferris, we will be very pleased to have you make your statement, and we will confine all statements to 5 minutes. The entire statement will be in the record and be available.

Mr. FERRIS. I appreciate that Mr. Chairman. But if it will not throw your schedule off, Mr. Gortikov and I had agreed that Mr. Gortikov would proceed first. Would that be permissible to you, Mr. Chairman?

The CHAIRMAN. That is all right, if he would prefer to go first.

STATEMENT OF A PANEL CONSISTING OF STANLEY M. GORTIKOV, PRESIDENT, RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC., NEW YORK, NY; AND CHARLES D. FERRIS, ESQ., OF MINTZ, LEVIN, COHN, FERRIS, GLOVSKY & POPEO, ON BEHALF OF THE AUDIO RECORDING RIGHTS COALITION

Mr. GORTIKOV. Thank you. Mr. Chairman, my name is Stanley Gortikov. I am president of the Recording Industry Association of America, and my organization, together with the Department of Professional Employees of the AFL–CIO, including musicians and vocalists unions, the National Music Publishers Association, and the Songwriters Guild of America, join together to endorse S. 1739 and urge you to approve it.

For many, it is difficult to understand how individuals taping albums in their own homes could cause such a stir in the music community, but home taping has become a way of life for millions—the standard way to acquire prerecorded music without paying for it.

The aggregate impact of those millions of people taping rather than buying the musical recordings which we sell is stunting our creative output, so that less and less new music is being released into the marketplace. It is limiting the career opportunities of recording artists, musicians, vocalists, songwriters, and the thousands of employees who depend on music for their livelihoods, and it is reducing musical choices available to the public.

For 5 years, we have been struggling to fashion an appropriate remedy to respond to this problem, only to find that the opponents of legislation deny that the problem even exists.

Of course, they deny it. To them, home taping is not a problem; it is a gigantic windfall. They sell the equipment which replicates our music and happily pocket the proceeds. Look at their advertisements up here.

They tout the abilities of their tape factories and tape collection expanders. "Save money," their ads say; "copy a friend's cassette," or by a machine that quickly "pays for itself" by turning inexpensive blanks into prerecorded cassettes.

In short, the equipment makers sell their products by encouraging others to help themselves to our products. This displaces the sales that are the record companies' only source of revenue—sales which are the lifeblood of the entire music industry.

S. 1739 is a reasonable and solely need legislative response to the radical displacement of sales caused by home taping. It calls on manufacturers and importers of audio recording equipment to share with the music community some of the revenues they have earned at our expense.

The bill also refects a major compromise—total elimination of the royalty on blank audio tape. This is a major disappointment to us, as it reduces by more than half the modest compensations we originally were seeking.

Nonetheless, we support this compromise, in the hope that Congress will finally take action to address this ever-worsening problem.

To illustrate the continuing threat of home taping, let me acquaint you with a brand new technology just introduced at the Consumer Electronics Show this past June—digital audio tape, or DAT.

In DAT, a minicassette, half the size of today's audio cassette—this revolutionary technology will carry perfect musical sounds much like compact discs do. But unlike compact discs, DAT will be able to record initially up to 2 hours of music on a minicassette, ultimately 4 to 6 hours of music.

With DAT, originals and copies all will sound alike; all will be perfect replications of each other. Therefore, with DAT, the displacement of sales caused by home taping is sure to experience a quantum leap as tapers produce their own master-quality recordings.

S. 1739 does not currently address the special problems raised by the new DAT technology. This bill was drafted before the introduction of DAT, so that the definition of audio recording device draws no distinction between these new DAT machines and the existing generation of analog tape recorders.

Clearly, the implications of this revolutionary recording technology are so significant that DAT machines should not be treated just like any other analog recording device. Indeed, since DAT machines have not yet been marketed, Congress has a rare opportunity to devise in separate legislation later a permanent solution to the digital home taping problem before severe incremental damage is caused by this new product.

In the meantime, the committee may wish to limit the application of the royalty provisions of S. 1739 to the kinds of recording devices that existed when the bill was originally drafted.

We implore this committee to act promptly on S. 1739. Further delay can only play into the hands of the Japanese manufacturers who, every year they delay congressional action, can sell another 20 million of their machines while the American music industry continues to reduce its creative output as it suffers from the sale displacement caused by home taping.

The time has come to end the equipment manufacturers' free ride. We need a legislative response to this problem and we ask that you help us achieve it. Thank you.

[The prepared statement follows:]

JOINT STATEMENT
OF
DEPARTMENT FOR PROFESSIONAL
EMPLOYEES, AFL-CIO
NATIONAL MUSIC PUBLISHERS' ASSOCIATION, INC.
RECORDING INDUSTRY ASSOCIATION OF AMERICA, INC.
AND
SONGWRITERS GUILD OF AMERICA

RE: S. 1739
THE HOME AUDIO RECORDING ACT

BEFORE THE
SENATE COMMITTEE ON THE JUDICIARY

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August 4, 1986

My name is Stanley M. Gortikov, and I am president of the Recording Industry Association of America, a trade association of recording companies which manufacture and distribute about 85% of the prerecorded music sold in the United States. I am pleased to testify today in support of the Home Audio Recording Act, as reported by the Subcommittee on Patents, Copyrights and Trademarks, and to submit this Joint Statement endorsing the legislation from the Department for Professional Employees, AFL-CIO, the National Music Publishers' Association, RIAA, and The Songwriters Guild of America.

Home Taping Is a Serious Problem

It has been five years now that we have been testifying before the Congress in search of an appropriate legislative response to the home taping problem. The first obstacle we encountered was skepticism -- skepticism that individuals taping albums in their homes for private non-commercial purposes could actually cause harm. But as has been shown by dozens of surveys in the United States[1] and around the world,[2]

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[1] See, e.g. , Audits & Surveys, "Home Taping in America: 1983 -- Extent and Impact," reprinted in Video and Audio Home Taping: Hearings Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. at 193-224

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economic studies of the U.S. recording industry by Dr. Alan Greenspan,[3] and in numerous hearings on the issue,[4] the seemingly innocuous practice of home audio taping is

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(1983); Warner Communications, Inc., "A Consumer Survey: Home Taping," reprinted in Copyright Infringements (Audio and Video Recorders): Hearings Before the Senate Comm. on the Judiciary, 97th Cong., 1st & 2d Sess. 775-826 (1981 & 1982); CBS Records, "Blank Tape Buyers: Their Attitudes and Impact on Prerecorded Music Sales," reprinted in id. at 848-64; Yankelovich, Skelly & White, Inc., "Why Americans Tape: A Survey of Home Audio Taping in the United States," reprinted in Home Recording of Copyrighted Works: Hearings Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary, 97th Cong., 2d Sess. at 927-1032 (1982); Warner Communications, Inc., "1981 Estimate of Loss Due to Home Taping: Tapers' Reports of Replacement" (April 1982); William R. Hamilton, "A Survey of Households with Tape Playback Equipment" (September 1979); The Roper Organization, "A Study on Tape Recording Practices Among the General Public" (June 1979); Warner Communications, Inc., "The Prerecorded Music Market: An Industry Survey" (March 1978).

[2] The studies have been undertaken in the following countries:

Australia (Reark Research Pty. Ltd., Taping Survey: A Draft Report Prepared for Australian Record Industry Association (March 1982)).

Austria (Oesterreichisches Gallup Institut, "Tonbandkassetten" (Sept. 1974)).

Belgium (Belgian Group of IFPA, Market of Recordings on Tapes and Cassettes (1978)).

Britain (Ernst & Whinney for British Phonographic Industry Ltd., Levy on Blank Audio Recording Tape (Draft - Jan. 1982)); British Market Research Bureau Ltd., Home Taping: Report on a Quantitative Survey (Jan. 1980); British Phonographic Industry Ltd., A Levy on Blank Video and Audio Tapes and Associated Hardware (July 1981); British Market Research Bureau Ltd., Home Taping:

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not innocuous at all: the aggregate impact of millions of people taping -- rather than buying -- the musical recordings we sell can threaten the economic foundations

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Report on a Quantitative Survey (Feb. 1982); British Market Research Bureau Ltd., Tape Recording - Report on a Quantitative Survey (Dec. 1973); British Market Research Bureau, Ltd., Tape Recording - Report on a Quantitative Survey (Nov. 1975); British Market Research Bureau Ltd., Tape Recording - Report on a Quantitative Survey (Nov. 1977); Economist Intelligence Unit Ltd., A Study of the UK Market for Blank and Prerecorded Audio Cassettes, Cartridges, and Tapes (1978); Annan Impey Morrish for the British Phonographic Industry Copyright Association, In Home Taping (1978).

Canada (Market Facts of Canada, Ltd., Survey on Purchasers of Blank Tapes: for Canadian Recording Industry Association (April-May 1980); Market Facts of Canada, Ltd., A Report on the Home Taping Practices of Canadians (March 1982); Gallup Poll of Canada, Gallup Audio Equipment Study (April 1980)).

Denmark (Nordic Research Association, Cassette Recording 1977 (Feb. 1977); The Danish Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway, and Denmark (Jan. 1980)).

Finland (The Finnish Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway and Denmark (1980); Gallup, Commissioned by TEOSTO, Gallup Poll of Home Taping (April 1979)).

France (SOFRES, Poll on Home Taping (May 1983); SOFRES, Survey: Recordings on Tapes and Cassettes (April 1976); SACEM, Intellectual Works Protected by Copyright - Private Copying (March 1979)); Louis Harris - France, The World of Music - Recordings of Discs on Cassettes (May 1980)).

Germany (The German Group of IFPI, et al., Market Research Survey Sponsored by GVL (1982); GFM/Gesellschaft fuer Marktforschung, Recording of Music onto Blank Cassettes (1980); The German Group of IFPI, GVL, Copying of Music onto Blank Cassettes (April

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of an entire industry, stunt its creative output, limit the career opportunities of recording artists, musicians, vocalists, songwriters and the thousands of

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1978)).

Japan (The Japanese Group of IFPI, et al., "Drastic Steps Urged To Save Record Industry," Mainichi Daily News (October 11. 1982); Electronic Association of Japan, Survey on Home Taping (1979); JASRAC, GEIDANKYO, and Japan Phonograph Record Association, Actual Survey on Private Recording (October 1976)).

Netherlands (Netherlands Association for the Phonographic Industry (NVPI), Home Taping: Investigation into the Making of Sound Copies on Tape and Cassettes by Individuals in the Netherlands in 1979 (Sept. 1980); SEO for STEMRA and NVPI, Survey on Private Copying (June 1976)).

New Zealand (Heylen Research Centre for the New Zealand Federation of the Phonographic Industry, Personal Tape Recording - A Study in Blank Tape Usage (Nov. 1976)).

Norway (Nordic Research Association, Cassette Recording 1977 (Feb. 1977); The Norwegian Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway, and Denmark (Jan. 1980)).

Sweden (Nordic Research Association, Cassette Recording 1977 (Feb. 1977); The Swedish Group of IFPI, et al., Gallup Survey Concerning the Music Recording Habits in Finland, Sweden, Norway, and Denmark (Jan. 1980)).

[3] Dr. Greenspan's studies have been reflected and summarized in his tesitimony before the Subcommittee on Patents, Copyrights and Trademarks on three occasions. See Statement of Alan Greenspan, reprinted in COPYRIGHT INFRINGEMENTS (Audio and Video Recorders: Hearings before the Senate Committee on the Judiciary, 97th Cong., 1st and 2d Sess. at 920-937 (1981 and 1982); Statement of Alan Greenspan Re S. 31, reprinted in Video and Audio Home Taping: Hearings Before the Subcomm. on
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people who depend on music for their livelihoods, and reduce the musical choices available to the public.

By voting to approve S. 1739, the Subcommittee on Patents, Copyrights and Trademarks recognized that home taping is indeed a serious problem, exacting huge costs from both the music community and consumers around the country. While tapers may get music virtually for free, the public as a whole picks up the tab. Home taping means:

-- Less investment in music, because it siphons off revenues that would otherwise be spent on new artists, new songwriters and new types of music. That's one of the reasons that, as RIAA statistics show, the

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[Footnote continued from previous page] Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. at 85-92 (1983); Statement of Alan Greenspan Re S. 1739, Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 99th Cong., 1st Sess. (October 1985).

[4] See, e.g., Hearings Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 99th Cong., 2d Sess. (March 1986); Hearings Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 99th Cong., 1st Sess. (October 1985); Hearings Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. (October 1983); Hearings Before the Senate Comm. on the Judiciary, 97th Cong., 1st & 2d Sess. (November 1981 and April 1982); Hearings Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary, 97th Cong., 2d Sess. (April-September 1982).

number of new albums released has plummeted by 43% since 1978.

-- Reduced support for less popular forms of music, because it dries up the funds recording companies and music publishers use to subsidize jazz, classical, folk, gospel, ethnic and other recordings that lack mass appeal.

-- More expensive music, because by reducing sales volume, home taping can force record companies to spread their cost of production over fewer albums, making each one cost more. Thus, those who buy will pay more so that those who tape can pay nothing.

-- Less incentive to create music, because it undermines the copyright system which is intended to reward creators for their labor and act as an incentive to future creativity. It deprives copyright owners of what is rightfully theirs, and diminishes their incentive to invest time, effort, and money in the high risk record industry.

The ultimate losers are the people who love music and, finally, music itself.[5]

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[5] The most recent comprehensive summary of the case for audio home taping legislation is set forth in the Joint Statement of the National Publishers Association, Inc., the Recording Industry Association of America, Inc. and The Songwriters Guild of America, submitted to the

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S. 1739 Is a Reasonable Legislative Response

The second obstacle we encountered in our search for a legislative response was the need to develop a suitable remedy. The Subcommittee has now crafted such a remedy, in S. 1739 as amended. To be sure, that bill does not go nearly as far as we would have preferred, but the compromise bill effectively reconciles the competing interests at stake in the home taping controversy:

It provides that consumers who tape copyrighted works in their homes for private, non-commercial use will not be liable for copyright infringement. In exchange, the bill requires importers and manufacturers of audio recording equipment to pay a reasonable, one-time royalty on each machine they sell to help offset the losses caused by home taping. After all, as their own advertisements show, manufacturers depend on the home taping of music to sell their blank tape and taping equipment. In essence, these manufacturers have found a way to appropriate to themselves the benefits of American musical creativity. Not only are they benefitting, but they are also damaging us in the process -- for when our music is taped instead of

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Subcommittee on Patents, Copyrights and Trademarks of the Senate Judiciary Committee on October 30, 1985.

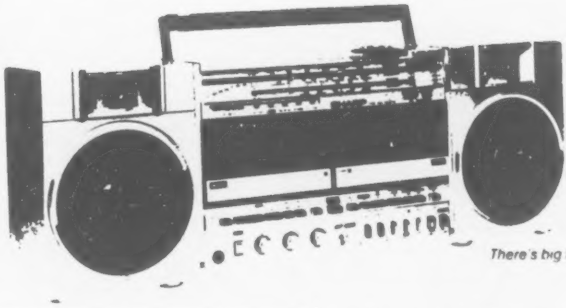
bought, the sales which are the lifeblood of our industry are displaced. Thus, the success of the tape and equipment manufacturers -- which is dependent on the vitality and appeal of our music -- comes at the direct expense of the American music community, and ultimately the American public. We are gratified that the Subcommittee agrees that it is entirely reasonable to expect those manufacturers and importers to share with us some of the revenues they have earned at our expense.

It is noteworthy that the royalty would be imposed on audio recording equipment only. It would not be imposed on equipment that can be used for video recording, thus eliminating any concern that the royalty would place any burden on video recording technology. Nor would a royalty be imposed at this time on blank tapes of any kind.

By establishing a series of appropriate exemptions, the legislation also ensures that those who purchase audio tape recorders for non-infringing purposes will not have to pay a royalty. Specifically, the royalty does not apply to audio equipment which can record only by microphone (e.g., dictation equipment) or which is otherwise unsuitable for music taping (e.g., voice quality machines); playback only equipment (e.g., many "personal stereos"); or equipment purchased for use in a trade, business, or comparable nonprofit organization. Most significantly, recorders equipped with a "decoder" which can permit or prevent taping of copyrighted recordings in accordance with special instructions encoded in the music (such as a "copy-code scanner," as described below), would also be exempt from royalty payments. Thus, equipment manufacturers could choose to sell audio recorders without decoders (for the purpose of copying musical recordings) and pay the prescribed royalty; or they can equip their machines with decoders, and thereby avoid the equipment royalty.

For those tape recorders not falling within one of the exemptions, the royalty rate would be:

- Five percent of the wholesale price for conventional audio recording equipment; and
- Twenty-five percent of the wholesale price of dual cassette audio recording equipment (which allows direct copying -- including high-speed dubbing -- of prerecorded tapes), in recognition of the intended use of such machines. (There cannot be any doubt about the purpose of these devices: advertisements for them urge consumers to "beat the system" and to "copy a borrowed cassette" with a machine that "quickly pays for itself by turning inexpensive blanks into prerecorded music cassettes." (See sample ads on the following pages.))



Tape Factory

There's big trouble in the music industry

One look at the Sharp Tape Factory and you can understand why there's trouble in the music industry Records aren't selling because people are copying their favorite songs from stereo FM radio stations onto inexpensive cassettes and playing them on everything from their Sony Walkman to their home cassette players The Sharp Tape Factory certainly won't help the recording industry

Equipped with AM/FM and two shortwave bands the Sharp has two high-quality cassette stereo recording tape decks The unit can record off any of its radio frequencies or an external turntable or duplicate an existing tape and do it at double speed A special high-quality audio dubbing circuit lets you speed up both cassette decks to duplicate tapes at one-half the time it normally takes And with tape deck to tape deck balanced circuitry your reproduction quality is awfully close to the quality you'd expect from a professional studio

If one of your friends has a tape you want to own copy it Or keep duplicate tapes one tape in your car and one at home Start a tape copying service Use the unit in your business to duplicate copies of important messages.

The Sharp Tape Factory makes sense if you're looking for a little more than entertainment from your home stereo cassette system

The two speakers don't separate from the main unit However, each speaker actually contains two separate speakers and they produce excellent sound for their small size The entire unit measures 5" x 8" x 22½", weighs 12 pounds, and comes complete with AC power cord There are provisions for 8 D-cell batteries (not supplied) and it has volume balance and tone controls A great music machine

Tape Factory (5051CA09 8 00) **$269.95**

> “ If one of your friends has a tape you want to own, copy it. Or keep duplicate tapes — one tape in your car and one at home. Start a tape copying service. Use the unit in your business to duplicate copies of important messages. ”

> “ One look at the Sharp Tape Factory and you can understand why there's trouble in the music industry. Records aren't selling because people are copying their favorite songs from stereo FM radio stations onto inexpensive cassettes and playing them on everything from their Sony Walkman to their home cassette players. The Sharp Tape Factory certainly won't help the recording industry. ”

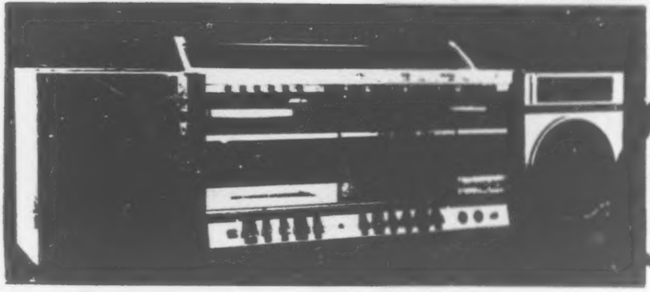
Beat the system. Copy your own cassettes.

Randix's two directly linked tape decks give you superb direct stereo tape copying capability in one unit. Duplicate a favorite tape for a friend or copy a borrowed cassette.

[illegible] built-in self-adjusting microphones [illegible] stereo. [illegible] with dramatic stereo separation. And the unique Continued Play feature automatically begins second tape when first one plays out. Plus you get a sensitive AM/FM tuner with AFC signal-locking for drift-free radio reception. With slide Volume, Bass/Treble and Balance controls, and inputs for extra speakers, turntable, or tape recorder. [illegible] phone jacks. Uses [illegible] batteries (not inclu[illegible] with AC cord. 90-[illegible] warranty. [illegible] FCC approved. [illegible]easures 14 × 7 × 6". Weighs 15 lbs.

The Randix portable studio recorder quickly pays for itself by turning inexpensive blanks into prerecorded music cassettes. It's like getting the high quality AM/FM stereo for free.

Randix Studio #LRX200 $199 (4.50)



Su[illegible]ed dubbing de[illegible]

Randix's new portable *high-speed* dubbing deck lets you make impeccable stereo cassette copies in *half* the normal time. Or tape your favorite radio programs directly from the sensitive built-in AM/FM tuner. Capture live [illegible] ingle [illegible] channel has its own built-in condenser microphone. It's a complete mini-studio for less than $150.

Each smooth front-loading tape transport is individually controlled, or can be set for continuous playback from Tape A to Tape B for up to 2 hours of uninterrupted music. Two 4" acoustic suspension speakers produce big, rich sound with dramatic stereo separation. Or use the stereo headphone jack for private listening. Rotary tuning, volume, tone and balance controls are conveniently placed for quick accessibility. 3-digit tape counter makes song location easy.

Pop-up carrying handle lets you take this compact (7H × 21W × 5D") [illegible] ABS, weighs 8½ lbs. UL approved. 90 day warranty. Turn inexpensive blank tapes into beautiful music — in half the time.

Randix Dual Cassette #JRX610 $149 (6.50)

Save Money—Copy A Friend's Cassette ◄

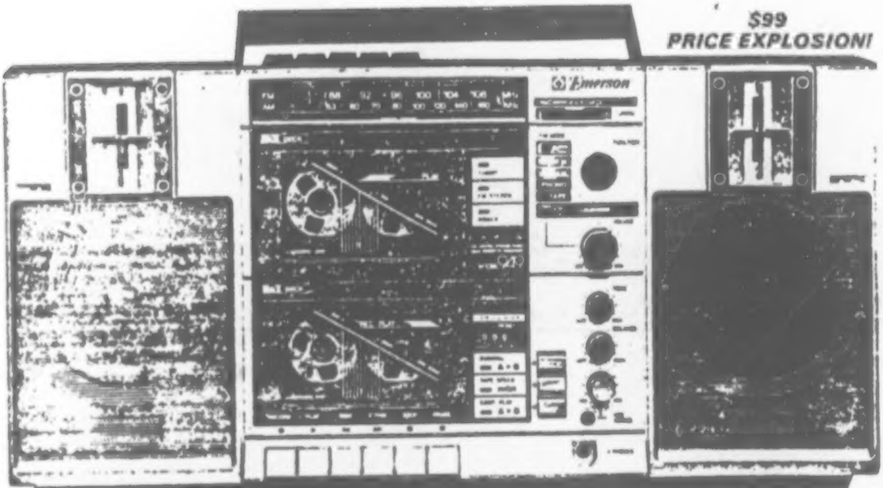
Randix's new twin cassette recorder allows you to copy any tape within minutes. And with its balanced tape deck circuitry, the reproduction approaches the quality obtained in professional recording studios.

A state-of-the-art continuous play function automatically activates a second tape once the first one is finished. So you have double the listening time, without the inconvenience of changing tapes. Two four-way speakers (6" woofers and 2" ceramic tweeters) produce vivid, full range stereo sound. Sensitive AM/FM tuner allows for distortion-free reception. Includes headphone jack, pause button, and a 3-digit tape counter. Plugs into any AC power outlet or uses 6 D batteries (not included). Weighs 14 lbs. UL approved. 90 day warranty.

Order this ultra-compact (21x7x6½") entertainment system today and begin saving money immediately by turning inexpensive blank tapes into high quality stereo cassettes.

■ Randix Twin Recorder SCR*610 $129(6.50)

$99
PRICE EXPLOSION!



Portable Cassette Factory

E[illegible] collecting into high gear with this all new high speed dubbing [illegible]ortable cass[illegible] duplicator a[illegible] AC/DC Stereo Music system.

You have friends. Your friends have friends. Why not pool your resources and dramaticially increase your cassette collection with the latest in high speed high quality tape duplicators.

[illegible] friend's house, at a party, or [illegible] collection [illegible] can play two cassettes in tandem for uninterrupted musical enjoyment, or enjoy great sounds from AM or FM stereo.

You can copy cassettes while operating from standard AC house current (AC cord included), or from batteries (not included). So, you can have great musical sounds or make copies wherever you are.

WHO SAYS
YOU CAN'T TAKE IT WITH YOU

Switch it on and you'll instantly hear the great sound quality that this system produces. But, wait till you hear the quality of the original cassette recordings and copies you'll make.

Just to test the quality of the copies, take your favorite tape, copy it, and then compare the difference. You'll be amazed at the crisp high quality of the new copy.

A note about Dolby®. If you have a tape recorded with either Dolby B or C, you can copy it on this deck and the copy will still be recorded in perfect Dolby. If you simply play a tape that's been recorded in Dolby, it will sound brighter and more vibrant than normal.

In fact, many people record cassettes in Dolby to play through their car stereos. What's really interesting, is that most car stereos don't have Dolby. But Dolby tapes make high-end starved car stereos sound more vibrantly alive because the highs in the recordings are boosted.

And, speaking of car stereos, this deck provides you with a great way of making duplicate tapes you can play in your car [illegible]use with your personal stereo.

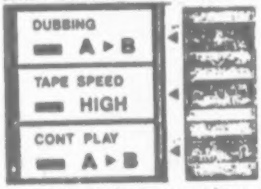
Now you can leave your original tapes safely at home, and let the sun, wind, and dust 'destroy' only your copies. So, you can both build your music collection and protect it with this new high speed dubbing Portable Cassette Factory.

And, you just may want to test the vibrant sound of a few tapes recorded with Dolby in your car. (Look at it this way, if you don't buy The Factory, you won't have read this ad for nothing.)

BUT IT'S THE MUSIC

Sure, you'll make copies, and sure you'll add to your collection. But most of the time, you'll simply want to hear beautiful music. And look at what you'll get.

First, you'll play beautiful music for a long time. When you push the Continuous Play button, the deck will allow you to listen to the cassette in Deck A, and then automatically switch to the cassette in Deck B for uninterrupted music.



If you're in the great outdoors, just push the Loudness Contour button and you'll hear the low depth of your music increase to fill your listening area.

If you sing, there's mike mixing. Just plug-in your own mike and you can add your voice to any tape you are recording.

You can select your choice of the sensitive AM or FM stereo tuners which really pull in and lock even weak distant stations, Tape, or an Aux inputs. Of course, you'll find all the standard controls including 'pause' on each cassette deck, a digital counter for the record deck, mono/stereo for FM and a headphone jack.

The Portable Cassette Factory is loaded with LED indicators that show virtually every function at a glance. And, with its full range speakers, it sounds as good as it looks. It's made by Emerson, and it's backed by their standard limited warranty.

TRY THE CASSETTE FACTORY
RISK FREE

Make some normal recordings when the The Factory arrives. Then take any cassette and duplicate it at normal speed. Finally, try the high speed dubbing.

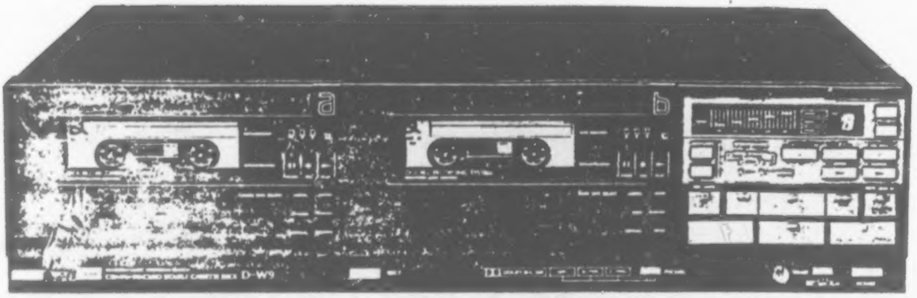
Listen to the crisp clean quality, not just of your cassettes but of the AM and FM stereo too. If you're not 100% satisfied, simply return it in its original box within 30 days to DAK for a refund.

To order your Emerson High Speed Cassette Dubbing, AM, FM Stereo Portable Cassette Factory risk free with your credit card, call toll free, or send your check for DAK's amazing multi-truckload purchase price of just $99 plus $6 for postage and handling. Order No. 9845. CA res add sales tax. Note: Massive shipments are scheduled to begin July 1.

Increase your tape library with the latest innovation in portable recording equipment. And enjoy great sounding music wherever you are, even at home.

DAK
INDUSTRIES INCORPORATED

TOLL-FREE ORDER LINE
For credit card orders call 24 hours a day 7 days a week
CALL TOLL-FREE. . .1-800-325-0800
10845 Vanowen St., N. Hollywood CA 91605



Tape Collection Expander

Copying tapes is the simplest thing this dual recording cassette deck with Dolby C, RMPS, and sequential record and play can do. It's much more than just two recording decks.

You're listening to FM. Suddenly you realize that a song you really like is being played. And unfortunately, you've already daydreamed through half of it.

Well, now you can build yourself a flawlessly recorded cassette collection of only your favorite songs almost effortlessly. Simply set this new relay recording dual cassette deck to record, 'tune-in' your favorite FM station, and leave.

When you return, you'll have one side of each cassette recorded with the music you missed. Then just start listening to the cassette in deck 'A'.

Whenever you hear a song you like, just touch one button and you'll compile a collection of tapes with just the music you like by copying them onto a blank cassette in deck 'B'.

And, wait till you hear the sound that these incredible decks produce. You're getting two true audiophile decks for less than the cost of just one.

A REAL DREAM MACHINE

It's the sound. The frequency response reaches 16,000hz with normal tape, 18,000hz with Chrome and 19,000hz with metal.

The signal to noise ratio is 58db without Dolby, 68db with Dolby B, and 78db with Dolby C. **But, look at this.** All these specs are for both decks, not just one.

You see, this all new dual cassette dream machine is really two separate cassette decks with 6 motors, and completely separate circuits housed in one dramatic high-tech black cabinet.

Wait till you use this deck. There's only one set of operational controls. You just push the 'A' or 'B' button before you push play, record, fast forward etc. And, if you want, just push the 'AB' button and both decks will spring to life.

To copy a tape, just put the recorded tape in deck 'A' and a blank cassette in deck 'B'. Then just push 'Dub'.

RMPS

And, speaking of automatic, this deck will search up to 15 different selections to find just the song you want. And, you can program it to play up to 3 songs in the order you choose. Of course, you can copy the selected songs as you listen.

SOUND ON SOUND

If you sing, this is the deck for you. Here's what you do. You can play a music tape on deck 'A', plug in a microphone and sing along while you record everything on deck 'B'.

Or, if you're really into professional applications, look at this. Record your own voice on either deck 'A' or 'B'. Then play the tape back in deck 'A' while you sing harmony to your first vocal.

Of course, you'll be recording your 'duet' on deck 'B'. Then take the tape from deck 'B' and put it in deck 'A' and repeat the process. Now you're a trio, then a quartet and finally a chorus.

With the incredible signal to noise ratio of this deck, you can really add on. Of course, you can do simple things like be a disc jockey and add your comments to any tape as it's being made. But singing along is really exciting.

DOUBLE RECORDING

In addition to the relay recording described above, you can make two identical recordings at the same time.

Each deck has a High-Bs hard permalloy head and a double-gap ferrite erase head. Each of the main transport motors is an electronically controlled DC motor for a maximum wow and flutter specification of just 0.04% (WRMS).

Each deck has a separate tape counter and each has automatic bias sensing. You can record Chrome in one deck and normal in the other automatically with no buttons to push. This is a very intelligent tape deck indeed.

And speaking of intelligent, it has a feature that is showing up more and more in high quality decks that I think we 'tape nuts' are just going to have to get used to.

This deck features Automatic Level Control for each deck. It does have a peak reading LED meter, but I think they put it in just to prove to us that it knows what it's doing.

And frankly, it does. You won't notice any of the dynamic range compression that I've always associated with automatic level control.

What you will notice is perfectly recorded tapes every time. I still miss the controls, but I must admit that the recording is flawless.

There is one recording level control. It's for the sound on sound mike recording. So, I guess they still need humans for something.

There's much more. You won't have to worry about where to start recording. Touch the tape 'lead-in' button and the deck will be automatically advanced past the leader.

If you have a timer, like the BSR system described on pages 3 to 5 of this catalog, you can set this deck to play or record when you are at work or asleep.

And, just one look at the control panel is enough to send the average astronaut into 7th heaven. There are mode indicators for virtually every function and audible indicators signal the actions.

The Tape Collection Expander is made by Sansui. It's their top of the line, and it sounds like it is. It is 17" wide, 4½" tall and 12¼" deep. They back it with a standard limited warranty.

EXPAND YOUR TAPE COLLECTION RISK FREE

Record from the most dramatic digital disk you own. Then listen to the tape. You'll be sold. Then copy the tape and listen to the copy. You'll find it hard to believe your ears.

You'll copy a friend's tapes, make fabulous live tapes and make spare tapes for your car and personal stereo. If you aren't 100% satisfied, simply return it to DAK in its original box within 30 days for a courteous refund.

To order your Sansui Tape Collection Expander risk free with your credit card, call toll free or send your check for DAK's breakthrough price of just $349 ($7 P&H) Order Number 9792.

Now you can have great music and total automation. And best of all, along with the audiophile quality, you can easily build a massive, totally personalized, tape collection that you'll enjoy for years.

The bill would also prohibit the sale of multiple well recording devices (i.e., tape recorders with three or more cavities for tapes or digital discs, which are capable of making more than one copy of prerecorded tapes simultaneously).

The royalties would be collected by the Copyright Office, and distributed by the Copyright Royalty Tribunal, in accordance with a detailed formula designed to ensure that all the participants in the music recording process share in the royalties and to maximize the incentives for further creative activity in the musical arts. In summary, the distribution formula now embodied in S. 1739

- Allocates 2% of the royalties, to be administered by the National Endowment for the Arts, for the benefit of aspiring musicians, vocalists and songwriters whose work has not yet been published or recorded.
- Distributes the remainder of the fund in proportion to the sales and radio airplay of copyrighted musical recordings, with certain adjustments that weight the distribution in favor of recordings in the lower 30% of the sales and airplay charts. This weighting

would provide additional compensation and incentives to those whose recorded work has not yet achieved widespread popularity, and thus serve one of the fundamental goals of copyright -- to encourage the creation of new music.

- Specifies a formula applicable to each recording that divides the royalty among the copyright owners of the sound recording (45%), the featured recording artist (30%), the composer/lyricist (11½%) and the music publisher (11½%) of the copyrighted musical work, and funds established for musicians and vocalists (2%).[6]

The Technological Alternative

Let there be no mistake about it, however: The Home Audio Recording Act, with all its virtues, does not solve the home taping problem. It simply ameliorates the negative impact of home taping to some extent, by providing some compensation for displaced sales. What we would gain from this legislation is but a fraction of what we are losing in displaced sales.[7]

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[6] The Joint Statement submitted to the Subcommittee on Patents, Copyrights and Trademarks at its hearing on March 25, 1986, by the Department for Professional Employees, AFL-CIO, the National Music Publishers Association, the Recording Industry Association of America and The Songwriters Guild of America, describes the distribution formula, and related administrative matters, in detail.

There is a way to solve the home taping problem -- by means of a new engineering invention that makes it possible to control unauthorized taping of copyrighted musical recordings. With this invention, which was demonstrated at a Subcommittee hearing on March 25, 1986, copyrighted records, tapes and compact discs can be encoded with an inaudible signal capable of being "read" by a special electronic scanning chip installed in audio recorders. Copyrighted music that is encoded would not be able to be taped.

The technology for this invention -- called "copy-coding" -- was developed and perfected by audio engineering experts at the CBS Technology Center. It has two elements, the encoder and the copy-code scanner.

- The encoder is a small electronic device that can "encode" any master recording (whether in digital or analog form) by intermittently removing from the music a tiny sliver of sound (beyond the highest notes of any musical instrument and between the notes of the musical scale). To create this "notch" in the frequency spectrum, the recording is simply passed through the encoding device electronically. The notch thus embedded in the recording is inaudible to listeners and does not affect the quality of the music.

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[7] That is why we were, of course, disappointed that the Subcommittee elected to eliminate the tape royalty entirely. That compromise reduced by more than half the modest compensation we were originally seeking -- which from the outset would never even have come close to making the copyright beneficiaries whole for the losses they incur as a result of home taping.

- The copy-code scanner is an integrated circuit ("IC") or chip designed to be built into the recording mechanism of any kind of audio recorder. When a record is taped, the copy-code scanner analyzes the music, looking for the encoded "notch" which is present only in "uncopiable" versions of copyrighted recordings. When the notch is detected, the copy-code scanner inhibits the recording function of the machine for a period of 25 seconds. The cycle is then repeated; if the scanner again determines that the notch is present, the recording function is interrupted for another 25 seconds. A copy taped from an "uncopiable" recording will thus consist of brief portions of music interrupted periodically by segments without sound.

The copy-coding technology is available for immediate implementation. Encoding devices have already been made for analog recordings, and encoders for digital recordings will be available in the very near future. Copy-code scanner chips will be on the market soon, and their cost will be nominal; the semiconductor chip is expected to cost less than $1 when mass quantities are produced. Should hardware manufacturers prefer to develop their own copy-code scanner chip, they would be free to do so. The specific design invented by CBS need not be prescribed -- only *performance* requirements must be met. In any event, CBS has pledged to license both its encoder and copy-code scanner on a royalty-free basis.

This technological solution to the home taping problem has great conceptual appeal, and the Subcommittee on Patents, Copyrights and Trademarks considered it carefully in determining how best to craft a legislative response. But as the Subcommittee apparently concluded, copy-coding is only a long-term solution. In the short term, royalties are needed to help offset the losses that home taping will continue to cause. This is because there are some 100 million recorders in American homes, and they will always be capable of copying *all* copyrighted recordings, whether or not they are encoded. Even if new machines were required to contain copy-code scanners, it would be so long before the existing machines cease to be used for home taping that a generation would pass before the beneficial effects of this legislation were felt. That is why we believe that the royalty approach embodied in

S. 1739 provides the most practical legislative response with respect to analog recording equipment.[8]

The technological solution does make sense, however, if it can be implemented before a new generation of recording equipment has been introduced. It is because an opportunity to effect this solution may now exist with respect to a new kind of recording equipment that we wish to bring to the Committee's attention the newest technological development confronting the music industry: Digital Audio Tape.

Digital Audio Tape

Digital Audio Tape ("DAT") is the tape version of compact disc technology. Like the CD, it carries sound frequency information in the form of a digital signal, which is laser read. Neither the tape, nor the machines necessary to play the tapes are yet available on the market, but several different models of DAT machines were just recently shown at the Consumer Electronics Show in Chicago in June. Thus, machines and blank tapes for consumer use can be introduced into the market at any time.

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[8] As previously noted, S. 1739 exempts from the royalty requirement any machines that are equipped with decoders. This provision enables equipment manufacturers to determine whether to sell audio recorders without decoders and pay a royalty, or to equip their machines with decoders and thereby avoid a royalty.

These machines will revolutionize existing taping technology. The tape cassettes will be about half the size of the analog audio cassette, yet they will hold up to two hours of music -- all with perfect sound fidelity. Sony is already predicting that a future generation of DAT machines will fit into the palm of the hand, and offer recording time of four to six hours.

The benefits of this new technology are exciting, but the damage it can cause is frightening. With DAT, the displacement of sales caused by home taping -- already at damaging levels -- is sure to experience a quantum leap. In essence, DAT will make possible digital-to-digital copying,[9] and it will significantly improve the quality of analog-to-digital home copying.

With DAT, there will no longer be any distinction between originals and copies; all will sound alike; all will be perfect replications of each other.

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[9] Prototype DAT recorders presently utilize a different sampling frequency for playback than recording, theoretically preventing digital-to-digital copying. In fact, however, there is nothing to prevent DAT hardware manufacturers from producing DAT machines which utilize the same sampling frequency for recording and playback. Nor is there anything to prevent the use of a frequency converter -- the technology for which already exists -- which will synchronize the sampling frequencies of players and recorders.

At present, record companies cannot offer their prerecorded music for sale on DAT cassettes, because the technology for the manufacture of prerecorded DAT cassettes has not yet been made available (and it probably will not be for another 1½ to 2 years). Only blank DAT cassettes will be sold. Thus, the current generation of DAT machines offers the music industry no new outlet for its prerecorded product; to the contrary, DAT machines can only reduce the sale of prerecorded product, as these machines can only be used for home taping.

And there can be little doubt that the manufacturers of DAT machines will market their product by touting the home taping capabilities of DAT technology -- that is, the ability to acquire perfect replications of musical recordings without having to pay for them.

That is why the advent of DAT has struck fear into the hearts of the music industries throughout the world -- fear that the practice of home taping will develop into a virulent new form as tapers gain the ability to produce their own master-quality recordings.

DAT and S. 1739

S. 1739 does not currently address the special problems raised by the new DAT technology. That bill was drafted before the introduction of DAT, so that the definition of "audio recording device" draws no distinction between DAT machines and any other kind of tape recorder.

Clearly, the implications of this revolutionary recording technology are so significant that DAT machines should not be treated like just any other analog recording device. The question is which legislative response to the home taping problem is the most appropriate for this new digital tape recording technology -- the royalty approach, or the copy-code alternative? If Congress were to prefer the royalty approach, it would necessarily have to consider: Should the royalty amount for DAT machines be the same as or greater than the royalties imposed on analog recording devices? Alternatively, Congress may prefer the copy-code alternative: Since DAT machines have not yet been marketed, now may be the time to establish the ground rules for this technology, before the machines have been purchased and consumer expectations have been established. Moreover, Congress now has a rare opportunity to write on a clean slate, to devise a permanent solution to the new digital home taping problem before severe damage is caused by this new product.[10]

In any event, the existing definition of "audio recording device" in S. 1739 should not be permitted to restrict the options available to Congress to devise a different response to the new digital home taping problem. To allow Congress the opportunity to tailor an appropriate legislative solution, it may be best to limit the application of the royalty provisions of S. 1739 to the kinds of recording devices that existed when the bill was originally drafted. That way, Congress can determine how best to deal with the new DAT technology in the future.

The Urgency of Legislation

Congress has now been studying the home taping problem for five years. The issue has been the subject of exhaustive testimony in numerous hearings. There have been countless surveys and studies.

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[10] The EEC is presently considering the use of copy-code technology to respond to the new generation of digital machines. Indeed, the EEC has already informally notified MITI (the Japanese trade ministry) that it is likely to require the installation of copy-code scanners in all DAT machines manufactured in, or imported into, the Common Market. The EEC will be deciding upon an official policy at a meeting of its Member States in September.

Meanwhile, the home taping problem grows more urgent every day. Each year millions of additional machines and hundreds of millions of new blank tapes are sold, causing additional harm to music creators and copyright owners.

The time has come to act. Further delay can only play into the hands of the Japanese manufacturers, who have publicly vowed to spend as much money as is necessary to defeat this legislation. For every year that they delay Congressional action, they can sell another 20 million or more machines, while the American music industry continues to reduce its creative output as it suffers from the sales displacement caused by home taping.

Nations throughout the world are already moving to protect their creative communities. Currently ten countries have enacted royalty legislation to respond to the home taping problem, and bills are pending in 12 additional nations. But the United States -- the home of the most creative music community in the world, and the source of half of the world's music -- does nothing.

The time has come to end the free ride taken by the manufacturers of recording equipment at the expense of American creators and copyright owners. We strenuously urge this Committee promptly to approve legislation -- to restore fairness to our copyright law, and to ensure the continued production of the new and diverse music that has always been a hallmark of the American cultural tradition.

The **Chairman**. Thank you very much.

I have got to go and open the Senate. Senator Heflin, who is ranking, you or Senator DeConcini?

Senator **Heflin**. He is ranking.

The **Chairman**. Could you take it for 15 minutes?

Senator **Heflin**. I imagine so.

The **Chairman**. Thank you very much.

Mr. **Ferris**. Mr. Chairman, do you wish me to proceed with my opening statement?

Senator **Heflin** [presiding]. Yes. Proceed.

STATEMENT OF CHARLES D. FERRIS

Mr. **Ferris**. Thank you. Mr. Chairman, members of the committee, my name is Charles D. Ferris. I am an attorney in Washington, DC, with the firm of Mintz, Levin, Cohn, Ferris, Glovsky & Popeo. I am here today representing the Audio Recording Rights Coalition.

Our coalition in a diverse group. It includes companies that are involved in the manufacture, sale and distribution of audio cassette recorders and audio tape and related equipment. Our membership includes many prominent trade associations, such as the Electronic Industries Association, the American Retail Federation, the National Retail Merchants Association, along with various consumer groups, thousands of individual retailers, educational organizations, and the American Council of the Blind.

Mr. Chairman, members of the committee, we oppose S. 1739, even in its modified form, and we welcome the administration's position today in not supporting S. 1739 and hoping to work toward a solution of whatever problem does exist in the future.

We find it is difficult to even conceive of this bill's serious consideration in these times of tax reduction and Gramm-Rudman-Hollings cutbacks. S. 1739 would enact a new tax, create a new subsidy for a single industry, an industry that has had record high profits the past 3 years.

But ignoring this remarkable swim against the tide of public policy, let me briefly put into another perspective the precise issues S. 1739 addresses.

First, when anyone copies a copyrighted work for commercial gain, it is a violation of the law, an act of piracy, and should be vigorously prosecuted. Our coalition strongly supports the vigorous enforcement of the law.

But home taping for personal use is not a violation of the copyright law. Thus, when I buy a phono record, take it home, play it on my turntable, listen to it, and simultaneously tape it on a blank cassette, preserving my newly purchased phono record as my master copy from the degradation that comes from each sequential play, the present law says I have done nothing unlawful.

When I purchase an album or a prerecorded cassette, take it home, tape from it my favorite selections and combine those selections with others from albums from my collection, thus customizing a tape of my personal favorites, the present law says I have done nothing unlawful.

When I purchase a record and combine it with other records and cassettes in my collection to make a 90-minute cassette so that I can play it in my car or on my Walkman, the present law says I have done nothing unlawful.

The question I hope this hearing will address is this: What activity is it that this committee wishes to make unlawful that the present law permits? The focus of the recording industry will be on the complications of fashioning a remedy, but a remedy for what?

Are audio recorders pernicious products? Are they of little redeeming value? A remedy that imposes a tax on their sale requires such a judgment. However, the recent history of the recording industry demonstrates to the contrary, that the audio recorder is the recording industry's best friend and has, in effect, rejuvenated the recording industry profits over the past 5 years.

The major uses of audio recording devices sold today have nothing to do with recording copyrighted material. Display 1 being put on the easel now shows just some of the diverse and personally creative uses that audio recorders can be put to.

Moreover, the audio recording equipment sold to the American consumer when used in conjunction with prerecorded music is overwhelmingly used for playback, not recording, and overwhelmingly to play back the music sold by the recording industry.

Even when this audio recording equipment is used for recording, not playing back music, the majority of the recordings are of music purchased by the person making the recording to put it in a format that will be more convenient and will permit fuller enjoyment of that purchased work.

So, again, I ask this committee to ask during this hearing and in its deliberations on S. 1739 which of these activities would you seek to declare unlawful, an infringement of the copyright law, that the remedy of S. 1739 would address?

I repeat this, Mr. Chairman and members of the committee, because the emphasis in considering this legislation has been on the remedy, and it is more than a complicated remedy. It is an unworkably over-broad remedy.

But I submit that this committee should not reach that question until it decides what presently lawful activity should be declared unlawful. It is only after that question is answered can this committee judge what the remedy should be.

The remedy of S. 1739 must be adjudged in the bill before this committee as over-broad unless this committee determines that listening is unlawful, for this bill places a tax, a penalty, on all equipment that has the capacity to record, regardless of the predominant and overwhelming uses of that equipment.

Display 2, which is up on this easel to my right, demonstrates some of the integrated uses of recorders in equipment ranging from television to boom boxes to integrated, sophisticated stereo systems.

I submit, Mr. Chairman, that upon reflection, this committee should overwhelmingly discard S. 1739 and declare it unwise, unjust, and unnecessary.

Thank you.

[Submissions of Mr. Ferris follow:]

STATEMENT OF CHARLES D. FERRIS
FOR THE
AUDIO RECORDING RIGHTS COALITION
ON S. 1739
BEFORE THE SENATE JUDICIARY COMMITTEE
Monday, August 4, 1986
10:30 a.m.

Mr. Chairman and members of the Committee, my name is Charles D. Ferris. I am an attorney in Washington, D.C. with the firm of Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C. I am here today representing the Audio Recording Rights Coalition ("ARRC").

Our Coalition is a diverse group. It includes companies that are involved in the manufacture, sale, and distribution of audio cassette recorders and audio tape, and related equipment. They include Tandy Corporation, 3M, G.E., Pfizer, DuPont, Memtek Products, Maxell, J.C. Penney, Sears, Roebuck & Co., Sony Corporation of America, and Matsushita Electric Corporation of America. Our membership includes many prominent trade associations, such as the Electronic Industries Association, the American Retail Federation, the National Retail Merchants Association, along with various consumer groups, thousands of individual retailers, educational organizations, and the American Council for the Blind.

The ARRC was formed in the summer of 1982. Our Coalition was formed because the Congress was receiving a lot of "facts" about audio home taping that we knew were wrong. Home taping was being blamed for the slump that the record industry was experiencing then. You heard testimony then that because of home taping no artist would ever again sell albums in the millions. How long ago that seems.

Today, despite the record companies' strong recovery, buoyed by new markets and a barrage of mega-hits -- most by people who were completely unknown in 1982 -- you are being asked to enact a royalty tax on all audio tape recorders. You are being told further that this drastic measure is somehow a "compromise" because the present version of S. 1739 does not include a tax on blank tapes as well. Senators, it reminds of the accountant who advises that when listing deductions for yourr tax return, you should put in everything, including the "kitchen sink." Then, if the I.R.S. should object, a "compromise" is available by offering to take out the "kitchen sink." I never believed the tax folks were so naive, and I don't think this Committee is naive, either. S. 1739 is no compromise -- it is still outrageous in what it proposes.

No Legislative Rationale for a Royalty Tax Has Ever Emerged.

Putting royalty taxes on audio tape recorders defies sound legal reasoning. We have heard about rights and about remedies, but never enough about why some rights should be trampled on to provide a "remedy" for others. Developments in the marketplace have made the case less, rather than more, persuasive, because they have shown that tape recorders enhance, rather than endanger, the commercial rights of record producers.

Back in 1971, Mr. Gortikov, for the RIAA, testified before a subcommittee of the House Judiciary Committee, on legislation that resulted in giving copyright protection to phonorecords.* He was asked, by a committee member, whether giving copyright protection to phonorecords, so as to prevent commercial piracy, would have any implications for private home recording. He answered:

> The pirate also argues that granting a copyright may raise questions about the individual who in his home may duplicate a commercial performance on home-recording equipment. We in the industry certainly have known that such amateur practices go on in the home, and we realistically recognize that no such enforcement is possible, and certainly none is intended.**

This is where things lay until the decision of the U.S. Court of Appeals for the Ninth Circuit in the "Betamax Case"***, which was subsequently overturned by the U.S. Supreme Court. The Ninth Circuit decision brought to the Congress recorder manufacturers, consumers and retailers asking for a legislative reversal; it also brought Hollywood executives asking for a legislative "settlement" through a tax on recorders, and one on blank tape, to boot. It was at this point that the record industry joined in, claiming that home taping was why their business had been bad.

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* Until the Sound Recording Amendment of 1971, records enjoyed no copyright protection at all.

** Hearings on S. 646 and H.R. 6927 Before Subcomm. No. 3 of the House Comm. on the Judiciary, 92d Cong., 1st Sess. 26 (1971).

*** Sony Corp. v. Universal City Studios, Inc., 464 U.S. 491 (1984).

You heard from the movie industry that the VCR was a new, hi-technology threat to its livelihood -- that when everyone had a VCR, nobody would go to the movies and no one would watch TV commercials. You heard from the recorder manufacturers that the VCR, like previous technological advances, was a golden opportunity for programmers astute enough to exploit it, and that it would turn out to be their "best friend." Now, about 20,000 video stores later, you have not seen a single legislative proposal in this Congress on video home recording. The evidence is simply too clear that the VCR is such an efficient video playback medium that its overall, net effect on Hollywood must be positive.

We also had a prescient decision from a Supreme Court that was unwilling to be swept along by fears that new technology is necessarily destructive of copyright interests. Its decision in the Betamax case was thoroughly considered and soundly reasoned. Nothing in the legislative debate, since, has laid a glove on it. The Court said that if a recorder has substantial noninfringing uses, you cannot invoke the doctrine of "contributory infringement" so as to make its seller liable for copyright infringement. In other words, it is simply contrary to our free market system to go around creating a "remedy" without first tying it closely and directly to some underlying right.

Audio Marketplace Developments

Just as the developments in the video marketplace have affirmed the soundness of the Supreme Court's judgment, developments in audio, and their effect on the record industry, have also amply illustrated that a royalty tax would be a remedy in search of a right.* It is scarcely a coincidence that in the last four years we have seen a burst of creativity in the market for audio equipment, and a renewed vitality in the recording industry, as well. To be sure, there are additional explanations for the recording industry revival -- new stars, new music, better management.** This industry has also tended to prosper or suffer in general accordance with the business cycle, and it suffered along with others in the recession of the early 1980's -- just as it has shared in the general recovery. But there is a direct, causal link between the new audio products and the new demand for music.

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* Unlike video copyright owners, no one in the recording industry has ever ventured to bring a lawsuit to test their rights with respect to home taping.

** See, Audio Recording Rights Coalition, Taxing Blank Tape and Recorders; Untimely, Unnecessary and Unfair 5-9 (July 1985).

Adding to the record industry's problems in 1980 was the fact that its prime customers were spending what disposable income they did have on new electronic products. Think of all the quarters that were spent on Pac Man, the ten dollar bills that went for video game cartridges, the hundreds of dollars spent on personal computers. Popular music, by comparison, was mired in disco, and in danger of becoming passe'.

Then came the Walkman. This audio product brought the glamor of high technology, so attractive in computers and video games, to music itself. It made the music so portable that ultimately it became irresistible. New technology also turned familiar "boom boxes" and car stereos into true high fidelity centers, at affordable prices. Another play-back bay was added to some boom-boxes and other recorders, so that tapes could be played sequentially and edited, and copies could be brought along to the beach. Car stereos now include tape decks and more speakers, and have supplanted yesterday's hi-tech favorite, the CB radio.

This infusion of technology did for audio what the VCR did for video -- it created a new market. Before these products arrived, the prerecorded tape was the stepchild of the recording industry. Issued with the lowest quality tapes and shells, released only for the most popular recordings of major artists, and usually sold under lock and key, it was a moribund product. Now, as record companies compile unprecedented years for sales and profits, these tapes in 1985 outsold vinyl phonorecords two-to-one; in 1986 the ratio is closer to three-to-one.

What changed? The quality of the cassettes themselves has scarcely changed. But ever so slowly, the record companies did begin to respond to the marketing opportunities offered by Walkman-type players and recorders, boom-boxes, car stereos, and improved, hi-tech home recorders. As Mr. Russ Solomon, President of Tower Records, put it:

> [T]he tape technology that came out of the recording machine resulted in the portable playback machine and the automobile machine, which created an enormous market for us.*

How did the new home recording technology create this market?

- Having a Walkman, boom-box or car stereo meant having immediate, portable access to your home record collection. It made people more interested in the music they already owned, which they could now enjoy more easily through home taping.

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* M. Goldberg, "The Wisdom of Solomon," Rolling Stone, Nov. 22, 1984 at 39.

- People purchased new music, knowing that no matter what the format, they could make a copy and take it with them, and could preserve their records from deteriorating.
- In buying new releases, it became most convenient simply to buy the prerecorded tape -- just as renting home videos became more convenient than taping off the air.
- Completing the cycle, the audio recorder at home became the basic playback unit for new purchases of prerecorded music. Once again, good marketing turned new technology into a friend.

Another hi-tech product to emerge from the research and development effort of recorder manufacturers is the compact disc player. There is no better illustration of the fact that, for the recording industry, new technology is friend, rather than foe.

The compact disc player, introduced a few years ago, uses digital technology to produce high quality performances from discs that are read by a laser beam. Although players, when they were introduced, cost around $1,000, production economies have brought the price down so that some models sell for close to $100 at retail. It has been estimated that the average owner of a compact disc player buys 30 to 40 discs per year.

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* "Hot Disc Players Going Fast," USA Today, Nov. 25, 1985, p. 1.

The recording industry severely underestimated the demand for compact discs, or CD's, and has not come close to catching up. The industry has been presented with -- and is trying to exploit -- the opportunity to sell consumers an entire new collection of their favorite music, in a superior format, as many consumers are buying CD's of music that they already own on record or tape.

In the short term, one consequence of the CD shortage, observed in trade publications, has been that many consumers have been unable to find albums they want on CD, so have been _holding off_ from buying those albums on phonorecords or tape.* Thus, the demand levels for prerecorded music over the last two years have certainly been understated, as they have been limited by the shortage of CD's. Record company sales and profits, nevertheless, have been at all-time levels over this period.

So you see, the Supreme Court's analysis in the Betamax case -- and Congress's appraisal of video recording technology -- were right on the money. The fact that tape recorders are sold does _not_ mean that they will be abused, rather than used, by consumers. The fact that something is new technology does _not_ mean that it is antithetical to copyright. The fact that the Recording Industry Association has been looking for a "remedy" does not mean that its members have any claim on the disposable income of consumers and the sales of recorder manufacturers.

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* See, _e.g._, "CD Consumers Want Unavailable Titles, But Won't Buy LP's," _Variety_, October 9, 1985, p. 117.

Most Recording Practices Are Not Harmful to the Music Business; Many Are Helpful

Let me make one point clear: the overwhelming majority of home taping is for the personal use and convenience of the taper and, when it is of prerecorded music, is of prerecorded music the taper already owns. Neither the RIAA nor anyone else has ever produced any evidence to the contrary. Studies commissioned by the RIAA have asked people misleading questions as to whether they "would have purchased" material they have taped. They compile absurd results for two reasons: first, because most taping is of selections, so there is no way the taper could have bought a comparable album; and second, the taper often answers that he "would have purchased" the music because, in fact, he already has. Results from such studies are then compiled and blown up by statistical methods that we have exposed as based on inconsistent assumptions and double counting.* The result is turned into huge dollar figures that bear no resemblance to reality. Moreover, the underlying studies are so old that they contain no data as to whether

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* See Nina W. Cornell, "Critique of 'Home Taping in America: 1983, Extent and Impact,' " Hearings on S. 31 Before Subcomm. on Patents, Copyrights and Trademarks, 98th Cong., 1st Sess. 419 - 435 (October 25, 1985); letter to Hon. Charles McC. Mathias, December 2, 1985.

"dual bay" recorders are used any differently from single bay recorders -- yet, a tax of 25%, rather than 5% is proposed. Where do these numbers come from?

Let us instead apply common fairness and common sense. Is it fair or sensible to expect consumers to pay the recording industry every time they tape to protect a record against scratching or warping? When they make a copy of a cassette to guard against the possibility of it being "eaten" by a car stereo? When they tape their own records or tapes so that they don't have to cart them between home and car, or to a second home? When they tape songs from several of their favorite albums to make a customized tape? We believe that consumers would, and should, answer "No, of course not."

Indeed, our own studies have shown that home taping often significantly stimulates purchases of prerecorded music. The Yankelovich survey showed that the majority of home tapers often or sometimes buy a record after they have made a home tape of part or all of it. Home taping has introduced two out of three tapers to musical artists or composers that they discover they like, and well over half have been prompted to buy records or prerecorded tapes after taping the artist's work. Moreover, Yankelovich found that home music tapers had recorded from over half of the records they bought in the previous six months, indicating that the ability to make home tapes of their records is part of the reason for buying these records in the first place. Despite all the anecdotes about "kids" and students, "heavy" tapers own approximately three times as many record albums and prerecorded tapes as "light tapers".* And since the introduction of "dual bay" recorders which supposedly are pernicious because they allow prerecorded cassettes to be copied, sales of prerecorded cassettes have gone from being below those of vinyl phonorecords to outselling phonorecords three to one.

The Tax Levied By S. 1739 Would Be Unjust For Many Reasons

In a nutshell, here is what S. 1739 would do. It would impose a royalty tax on the first wholesale sale** of any recorder. The rate, for the first five years, would be 5% for all devices containing a single tape deck, and 25% for devices containing two bays, even if one of the bays only plays back. After five years, the tax rate would be set at the unfettered discretion of the Copyright Royalty Tribunal -- one of the most troubled and understaffed agencies in Washington.

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* See testimony of David Richardson, Vice President, Policy Planning Group, Yankelovich, Skelly and White, Inc., before the subcommittee on Patents, Copyrights and Trademarks, Senate Judiciary Committee, Hearings, *supra*, p. 438.

** For fully integrated sellers like Tandy, the tax would be computed on the retail sales price, even though it would still be assessed at the manufacturing level. See testimony today of John V. Roach, Chairman, Tandy Corp.

Because the tax is assessed at the very top of the distribution chain, it would be certain to be passed on to all successive levels, with customary markups, until paid by the consumer. Please note -- this will be the case no matter what intended or actual use he or she will make of the recorder. I can only begin to catalog the many ways in which this would be grossly unfair:

Recorders put to uses that have nothing to do with pre-recorded music would still be taxed. The study by Yankelovich, Skelly & White* revealed that just over half of all home recordings have nothing to do with prerecorded music. If you are skeptical of this finding, please look at Display 1, and the great diversity of the audio recorders shown there. Because people -- especially students and children -- are creative, and they have grown comfortable with recorders, they put them to many personal uses that have nothing to do with the recording industry's product. Yet, the record companies, through S. 1739, would get their cut every time one of these people buys a recorder. Two of the most severely affected groups are represented on other panels today. Musicians have great need of recorders, especially the newer "dual decks" that allow them to make demonstration copies. Yet these would be taxed at 25%. And, of course, the blind, who rely on recording devices for a number of purposes, would have to pay.

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*/ Audio Recording Rights Coalition, Why Americans Tape, September, 1982

Recorders used exclusively or primarily to play back the record industry's product still would be taxed. This might have been a relatively minor consideration even five years ago, but because prerecorded tapes now dominate sales, S. 1739 would now be taxing the primary playing instrument for the recording industry's own product*

Recorders used to make recordings for the car, the beach, and the Walkman, and to preserve phonorecords still would be taxed. This is what the majority of all home taping of prerecorded music is all about.** When I buy a book I can enjoy it at home, at the beach, or on the park bench. Why should I pay a tax on the recorders that let me enjoy my record collection the same way? This is double payment for the music I have bought, just because I want to enjoy it more conveniently, in a different physical format.

A tax on recorders is grossly inefficient in almost every economic respect.

> First, as an economist with the Justice Department's Antitrust Division pointed out in an April, 1986 paper, the tape recorder, viewed as a metering mechanism for the use of prerecorded material,

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* Under any theory of "contributory" harm, especially that stated by the Supreme Court in its "Betamax" decision, machines that so clearly help the industry should not be taxed.

** Yankelovich Survey, p. 54.

is an abysmal failure.* In other words, even if your sense of rough justice is not offended by taxing everyone, it should still be offended by levying the tax on recorders, because recorder purchases provide the worst possible measure of how much copyrighted material is copied.

Second, a tax on recorders distorts new technology. To give just one example, today virtually all "boom boxes" have recording capability, even though they are used primarily for playback. These inexpensive recorders are most likely to be used for personal recording, such as that done by children and students. Yet a tax levied on the entire value of the boom box could cause the manufacturers to remove this recording capability -- accomplishing nothing with respect to prerecorded music but ruining a very constructive feature. Perhaps of more serious long-term consequence is the fact that a tax on audio recording capability will prevent the integration of audio, video and data capabilities in new products. Such products are already on the way, and should be of great utility -- if S. 1739 does not pass.

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* See Timothy J. Brennan, Taxing Home Audio Taping, Economic Analysis Group Discussion Paper EAG 86-6, Antitrust Division, U.S. Department of Justice, p. 22 (April 15, 1986)

Third, we have received many letters from people who are concerned that S. 1739 would deprive them of freedom of choice as to what music, and which musicians, they wish to support. Today, those who are distressed with the direction of popular music need not buy it. Once S. 1739 passes, however, whenever anyone buys a tape recorder -- and we have found in mail we have received that recorders often are used in missionary work -- that individual will know that a certain percentage of the price will go to a commercially successful group that he or she may think is an abomination. But, because S. 1739 taxes all recorders, and divides most of the proceeds according to album sales, the only way to avoid contributing to that group's support is to avoid buying a tape recorder.

The Purported Exemptions in S. 1739 Are Only Shells and Shams

Confronted with all the unfairness and distortions that S. 1739 would cause, its backers reply that these would be alleviated or ameliorated by various "exemptions." Nothing could be further from the truth -- these "exemptions" exist on paper only. The problems, in the real world, will remain.

Integrated units. Please refer to Display 2. Shown here are but a few examples of the way audio tape recorders are integrated into other products, rather than sold separately: rack systems, compact units, boom boxes, table radios. The tax would be levied on the total value of these systems, rather than on the recorder portion alone. The drafters have not even tried to put in a paper exemption on this issue -- probably because this would make all too obvious the attendant problems of assigning a value to the recorder portions, keeping such information confidential, and avoiding litigation over the result.

This problem is even worse with respect to "dual decks," which are taxed at 25%. And the height of absurdity is reached in the treatment of any unit containing a dual deck and a compact disc player -- it would be entirely banned.* This shows the fallacy of attacking product integration, because when you put a CD player into a boom box, you enhance its playback use and lessen the incentive to tape.

Business or Nonprofit Use. There is a paper "exemption" for recorders purchased for business use or by a non-profit organization [(c)(D)(i)] that, if invoked at all, could only work in a destructive manner. How could any purchaser receive a "rebate" for a tax paid by someone five steps above him in the distribution system? One way is to sell recorders for business or non-profit use only through a separate distribution cartel. This freezes out any retailer or wholesaler who wishes to compete for this business. Aside from unfairly injuring the retailer, it forces non-profit organizations to form purchasing collectives if their members wish to avoid the tax.

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*/ See definition of "multiple audio recording device" [(d)](6)]. Adding the CD player is banned because a player of a "phonorecord in any digital or any tape format" may not be integrated into a dual recording device.

The alternative is to require that the retailer himself give the rebate, then process a voucher for a refund from his distributor, who gets a refund from the wholesaler, who gets a refund from the manufacturer, who applies for a refund to the Copyright Royalty Tribunal. If the Tribunal then questions the validity of a voucher, back down the chain we go. And this raises an interesting question: What must a purchaser offer, or prove, to obtain a rebate? How thorough an investigation must the retailer make?* If he has a significant duty, his sales people will have time for little else. If he has a minimal duty, the opportunities for allegations of fraud, and for litigation, are immense.

"Unsuitable for Private Recordings" S. 1739 also contains a paper exemption for devices "unsuitable for making audio recordings by individuals for private use." [(c)(C)] There has been ample testimony that this category is necessarily arbitrary, so any line drawn to enforce it can only have a chilling efect on technological integration.* Again, a provision is not really an "exemption" when any effort to enforce it will do more harm than good.

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* S. 1739 also requires a determination that a business or nonprofit purchaser will not use the recorders for private use. How can the retailer ascertain this? Must he demand an affidavit?

Finally, we are told that the faults, flaws and unfairness of S. 1739 can be avoided through the "decoder chip" provision. The bill says that if a manufacturer sells a recorder with a device that, in conjunction with encoding in prerecorded material, can prevent copying, the manufacturer need not pay the tax on that device. However, S. 1739 contains no requirement either that manufacturers insert the chip, or that the record companies put the code in their products, or, if they do, that they also make unencoded products available on reasonable terms. The subcommittee held a hearing as to how such a system might really work, and how the bill might be changed to spell this out. The result was that the decoder chip provision was not spelled out or modified at all. This allows proponents to tell some people, who think the tax is unfair, "Don't worry about the tax; it's a chip bill," while telling others, who are horrified by the chip idea, "Don't worry, we never really did anything about it."

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* See statements of Leonard Feldman and Edward Foster before subcommmittee on Patents, Copyrights and Trademarks, October 30, 1985.

The truth is that this provison spells chaos for all sellers and buyers of recorders, and threatens the ability of smaller record stores to compete with the large ones. Once this bill is enacted, if any manufacturer sees fit to sell a recorder with a chip in it, the retailer who sells the recorder, and his customers, will have no idea how valuable this recorder really is. No one will know whether the record companies will adopt encoding, and if so, whether unencoded versions will be made reasonably available at reasonable prices. There is no way for consumers to compare these recorders with identical but higher priced versions without chips, on which the tax has been paid, or with the 138.2 million recorders they already own. There is no way for them to know whether they will continue to enjoy the right to record music they buy, or not. This is not a "marketplace solution" for anyone concerned -- it is the opposite.*

For small record retailers, widespread sales of decoder chip recorders pose an equally grave threat. If record companies do not make a second inventory of unencoded versions available in reasonable quantities, these will have to be specifically ordered. If an adequate second inventory is made available, it will have to be stocked and displayed. For the small retailer with limited shelf space, this means further cutting down on the number of titles he can stock, particularly in highly selective areas, such as jazz and classical -- so his ability to compete with the large record chains -- already gravely threatened -- is further reduced.

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* The marketplace is further threatened by the opportunity for the record companies to use the contemplated price differential between encoded and unencoded versions as a facilitating device to charge a uniformly and unreasonably large premium for the unencoded versions that can be recorded.

Ironically, this "squeeze out" effect of an additional inventory of records, tapes and discs also means much less opportunity for the marginal artists whose plight is cited by the R.I.A.A. as one reason for passing S. 1739.*

Mandating the use of decoder chips, as a "solution," would make matters even worse. Manufacturers and retailers would be forced to offer products that lack an important capability compared to those they already own. Indeed, decoder chips would do for old tape recorders what the Mexico City taxicab market has done for old Oldsmobiles. But for retailers trying to sell new tape recorders, this is no joke. Is this the sort of marketplace -- where the old is better than the new -- that we want?

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* The claim that record companies would use returns from any royalty tax to subsidize marginal artists is condemned as "specious" from an econcomic point of view in the paper by Justice Department economist Brennan, supra, p. 28.

CONCLUSION

Mr. Chairman, there is no reason at all for S. 1739 to become law. The sellers of tape recorders, and the individuals who buy them for private home use deserve to be left in peace. The new technology that these recorders represent has, in fact offered a host of remarkable opportunities to the recording industry and the artists who are dependent on it. Some of these opportunities have been successfully exploited; others have been seized only slowly, but the result is clear. New technology has helped save the music business. The claims that home taping has hurt sales are based on misleading and self-serving data; the evidence that tape recorders support the record industry's present prosperity is clear for all to see.

It would be grossly unfair to enact this tax. It forces people to pay, now matter how they use their recorders, whether they use them only for playback, indeed whether they ever tape prerecorded music at all. It cuts across every effective link, in the marketplace, between peoples' desires and how their money is spent -- even to the extent of forcing individuals to support and encourage public personalities of whom they personally disapprove. The "exemptions" don't even address the most serious problems, and only paper over or make worse the ones they do address.

Mr. Chairman, there is simply no need to call down on the heads of the American public all the problems, the unfairness, the inconvenience, and the bad precedent represented by S. 1739.

Thank you for having invited me to appear today.

DEFENDING AUDIO RECORDING RIGHTS

Audio Recording Rights Coalition
2001 Eye Street, N.W.
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August 1986

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I. Introduction

The recording industry, piggybacking on demands for a copyright royalty made by the motion picture industry,[1] in 1982 began a campaign for royalty taxes on audio recording equipment and blank tapes, claiming that home audio taping causes millions of dollars of damage to it. Several bills to impose such taxes have been introduced since then, and two bills currently pending, S. 1739 and H.R. 2911, again propose such taxes. The amended version of S. 1739 now before the Senate Judiciary Committee is no improvement over earlier proposals.

This legislation would force the American public to pay hundreds of millions of dollars annually to the recording industry. The Audio Recording Rights Coalition has vigorously opposed, and continues to oppose, any proposal that would impose a new home taping tax on millions of consumers. In particular, the Coalition rejects any attempt to characterize the amended version of S. 1739 as a compromise.[2]

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[1] For discussion on the home video taping issue, see "Home VCR & Copyright," issued in April 1982 by the Home Recording Rights Coalition.

[2] The amended version of S. 1739 presently does not impose a tax on blank audio tape. The recording industry, however, is intent on taxing audio tape as

Ever since 1971, when Congress exempted home audio taping from copyright liability, millions of Americans have taped at home as a way of enhancing their enjoyment of music. During this period there has never been the slightest intimation that what they were doing was illegal. With its royalty tax proposals, the recording industry, however, is now asking that consumers pay for doing merely what they have done for fifteen years.

Although the recording industry claims that home audio taping injures copyright owners and, as such, compensation is warranted, its arguments simply do not fit the facts. First of all, an enormous percentage of all home recording does not even involve copyrighted material. Yet, such taping practices would still be subject to a royalty tax. The royalty proposals are, therefore, seriously overbroad, indiscriminately taxing the bulk of audio taping that involves uncopyrighted family, educational, and business recordings along with the minority of taping that is of copyrighted material.

[footnote continued]

well as recorders and the Coalition believes that there may well be an attempt to amend S. 1739 to reintroduce a tape tax. Thus, throughout this paper, where there are references to home taping activity, the primary, but not sole, emphasis is on audio recording equipment.

Moreover, the recording industry proposals treat all home taping alike. There is, however, a wide diversity in home taping behavior. Much home taping is from tapers' own collections -- music that they have already purchased. In addition, tapers create customized selection tapes of their favorite music, tapes that are not, by definition, commercially available. Many collectors tape to preserve rare or other valuable records. None of these practices are intended to avoid the purchase of prerecorded music or harm the recording industry. Any coerced payment by home tapers who tape music they have already bought and paid for would be, quite simply, double compensation to -- and an entirely unjustified windfall for -- the record companies.

Furthermore, far from displacing sales, much home taping behavior actually stimulates purchases of prerecorded music. Indeed, an important element of a consumer's decision to purchase prerecorded music is the ability to tape it. Surveys reveal that there is a synergistic relationship between taping and purchasing music: the more prerecorded music people buy, the more likely they are to tape, and the more they tape, the more likely they are to buy more prerecorded music.

Given the reluctance of the recording industry to embrace technological developments, it is not surprising that its proposals utterly fail to acknowledge the extraordinary benefits that it -- and the entire creative community -- have realized from the very products that it seeks to tax. Technology is among the industry's greatest friends: the cassette recorder and the personal and portable stereo have created vast new markets for the record companies and have benefitted significantly the entire creative community. The compact disc player is about to generate even greater markets for the industry -- if it does not miss the boat. Cumulatively, then, taping and recording technologies have poured literally billions of dollars into recording industry coffers.

Although the industry likes to blame home taping for its so-called "lost" sales in the early 1980s, the current boom in record company sales and profits demonstrates the extent to which taping was never anything more than a scapegoat: there is now ample evidence that whatever had plagued the industry ails it no longer. The economy has improved over the last three or four years; the videogame fad that had siphoned millions of dollars from record sales has gone bust; new promotional tools, such as music video, are available;

and record companies have recognized that prudent financial and artistic policies can make a major difference in their bottom lines. In sum, the industry is back -- its cries for financial relief from home taping now ring hollow.

Further, a royalty tax would not help the "struggling" artists and composers for whom the industry proclaims such sympathy. A few entertainment conglomerates and a handful of singer/songwriters, who are already well compensated, would be the primary beneficiaries of an audio tax. The structure of the industry, and the historic tension between artists and the record companies, strongly suggest that very little, if any, of the tax monies would ever trickle down to the creative talent. Hence, despite the distribution scheme of the amended version of S. 1739, the recording industry would retain the power to negate any financial benefits that struggling artists would reap.

S. 1739 is itself so rife with massive flaws that the cost and difficulty of implementation would be enormous. As an initial matter, however, it is obvious that the amounts of the levy bear no relation either to the amount of home taping, or to any actual harm therefrom. Moreover, the method for exempting certain business or other "non-infringing" users of recorders and tapes is far too cumbersome to work. Similarly, the complex procedure for allocating and distributing funds to claimants, which relies on the discretion of the Copyright Royalty Tribunal, will create a legal and administrative morass that will cause delay and necessitate constant revisiting by Congress. Finally, the notion of a royalty tax on hardware brands equipment manufacturers as "contributory infringers" and essentially overturns one of the fundamental holdings of the Supreme Court's 1984 decision in Sony Corp. v. Universal City Studios.

Prudence and efficiency militate against congressional enactment of an audio tax. The recording industry has rebounded completely, surpassing previous highs. Moreover, the recording industry has at last recognized a number of its marketing mistakes and is moving quickly to remedy them. These changes will likely spur additional sales. Last, impending technological changes that are expected to alter the way music is produced, promoted, marketed, and distributed may eliminate home audio taping as we know it today, thus rendering any royalty an anachronism.

II. Congress Has Exempted Home Audio Taping From Copyright Liability

In 1971, Congress established, for the first time, a limited copyright in sound recordings.[3] At the same time, the legislative history demonstrates congressional intent to recognize expressly the legitimacy of private audio taping and exempt it from copyright liability.[4] Since then, tens of millions of Americans have enjoyed taping at home. Today, there is no more reason to deem the practice illegitimate than there was at the time. By forcing consumers to pay a royalty tax, Congress would be rescinding rights of the public that have been virtually codified for fifteen years.

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[3] The Sound Recording Amendment of 1971, Pub. L. 92-140, 85 Stat. 391 (1971) [hereinafter cited as "1971 Act"]. Granting copyright owners of sound recordings the exclusive right of reproduction was intended to combat commercial record piracy. See H.R. Rep. No. 487, 92d Cong., 1st Sess., reprinted in [1971] U.S. Code Cong. & Admin. News 1566. Consistent with the narrow objective of putting a stop to commercial piracy, Congress chose not to give owners of copyrights in sound recording the right to receive "performance royalties" when their sound recordings are played on radio, television, in a jukebox, or in a live public performance. Since then Congress has refused to increase copyright owners' control by granting a performance royalty for sound recordings, despite repeated requests by the recording industry.

Sound recordings are separate from the underlying musical works of which they are comprised. "Sound recordings" are defined in the statute as follows:

> "Sound recordings" are works that result from the fixation of a series of musical, spoken, or other sounds, but not including the sounds accompanying a motion picture or other audiovisual work, regardless of the nature of the material objects, such as disks, tapes, or other phonorecords, in which they are embodied.

Composers, authors, and publishers have long enjoyed copyright protection for their works -- as "musical works" -- to be distinguished from "sound recordings," which include their contributions, as well as those of performers and record producers.

The General Revision of the Copyright Act in 1976 incorporated the legislative history of the 1971 Act, including the exemption for home audio taping.[5] Undergirding such legislation is the fundamental proposition that copyright is intended to generate incentives that are sufficient to motivate creators to produce works for distribution to the public; it is, then, the interest of the public that is preeminent.[6]

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[4] The final House Report on the 1971 Act declared unequivocally that Congress did not intend home taping to be an infringement:

> Specifically, it is not the intention of the Committee to restrain the home recording, from broadcasts or from tapes or records, of recorded performances, where the home recording is for private use and with no purpose of reproducing or otherwise capitalizing commercially on it. This practice is common and unrestrained today, and the record producers and performers would be in no different position from that of owners of copyright in recorded musical compositions over the past twenty years. [emphasis added]

H.R. Rep. No. 487, supra note 3, at 7, reprinted in [1971] U.S. Code Cong. & Admin. News at 1572.

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[5] Some in the recording industry now argue that Congress, by not repeating in the House Committee report that accompanied the 1976 Act the paragraph set forth in note 4, thereby revised its views with respect to home taping and, suddenly, in 1976, turned tens of millions of citizens into lawbreakers. *See, e.g.*, Recording Indus. Ass'n of America, Inc., "Audio Home Taping: The Case For A Fair Deal for Copyright Owners and Consumers" 28-30, *reprinted in Copyright Infringements: Hearings on S. 1758 Before the Senate Comm. on the Judiciary*, 97th Cong., 1st & 2d Sess. 737-39 (1982) [hereinafter "*Hearings on S. 1758*"]. It is asserted that this was done even though nothing was said to alert the public, and even though there was no change in those circumstances that had led Congress to express clearly and unequivocally its intent in 1971. Quite simply, because the issues were firmly resolved in 1971, there was no need for any further discussion in 1976, and the absence of the paragraph was, therefore, of no significance. In any case, if the law *was* changed in 1976, the recording industry has no need for further change. There is nothing in the Supreme Court decision in *Sony Corp. v. Universal City Studios* to the contrary. First, the majority opinion expressly does not address the applicability of the 1971 Act because it finds that home videotaping is a "fair use" under Section 107 of the Copyright Act. *See* 104 S. Ct. 774, 783 n.11 (1984). To the extent the dissenting opinion addresses the legislative history of the 1971 Act, moreover, it does so in the context of home videotaping, as to which it concludes that the 1971 Act is not relevant.

[6] *See infra* Section III.B.1. (discussing balance in copyright law).

In striking the proper balance between the interests of creators and the public, Congress has always had, and continues to have, good reasons for exempting home audio taping from copyright liability. The exclusive right of reproduction conferred on copyright owners is solely aimed at protecting their monopoly against commercial reproduction and distribution. Home taping, however, is entirely noncommercial and merely enhances consumer enjoyment. Home taping also can serve a variety of educational and business uses. Policing home taping would be extremely difficult and intrusive. Home taping behavior can stimulate the sale of prerecorded music. Simply stated, the recording industry did not show -- and still has not demonstrated -- that home audio taping hurts copyright owners.[7]

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[7] In 1971, Stanley M. Gortikov, President of the Recording Industry Association of America, Inc. ("RIAA"), made the following statement to Congress:

> The pirate also argues that granting a copyright may raise questions about the individual who in his home may duplicate a commercial performance on home-recording equipment. We in the industry certainly have known that such amateur practices go on in the home, and we realistically recognize that no such enforcement is possible, and certainly none is intended. [emphasis added]

Hearings on S. 646 and H.R. 6927 Before Subcomm. No. 3 of the House Comm. on the Judiciary, 92d Cong., 1st Sess. 26 (1971).

For all these reasons, it is clear that home audio taping should remain exempt from liability. Absent the most compelling showing to Congress, it would be unjustified and unfair to tax the public for behavior that, historically, has been completely legitimate.[8]

III. A Royalty Tax Is Unjustified Given The True Nature Of Home Audio Taping

A. Taping Of Prerecorded Music At Home Is Not Harmful To Record And Prerecorded Tape Sales, And Is Often Beneficial

Contrary to what the recording industry would have Congress believe, home taping is, by and large, independent of sales of prerecorded music, or actually stimulates such sales. There are no meaningful data from which Congress could conclude that home taping has a sufficiently adverse economic impact on the recording industry to justify compensation -- let alone compensation from royalty taxes collected through a compulsory licensing scheme. Proponents of royalty taxes on audio recording equipment have argued -- mistakenly --

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[8] If, indeed, the recording industry believes that home taping, under current law, constitutes copyright infringement, it has had ample opportunity to test its contention in court; however, it has not yet instituted a single such case.

that home audio taping displaces sales of records and prerecorded tapes. The underlying assumption of that argument is, however, not supported by the facts.

A full-scale survey of home audio taping in the United States was conducted in July 1982 by Yankelovich, Skelly and White, Inc. ("Yankelovich Survey") for the Audio Recording Rights Coalition. The study was reported as "Why Americans Tape: A Survey of Home Audio Taping in the United States."[9] The Yankelovich Survey findings are, moreover, confirmed by data from the recording industry's own earlier surveys of audio taping.[10] Some of these findings are that:

- The majority of material that consumers tape is not copyrighted music.

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[9] The full published report of the Yankelovich Survey, including the survey questionnaire and methodology, is available from the ARRC: 2001 Eye Street, N.W., Washington, D.C. 20006.

[10] The recording industry surveys include: Audits & Surveys, "Home Taping in America: 1983, Extent and Impact" (Oct. 1983) ("Audits & Surveys") (prepared for the Recording Industry Association of America, Inc.); Warner Communications, Inc., "A Consumer Survey: Home Taping" (Mar. 1982) ("Warner Survey"); CBS Records Market Research, "Blank Tape Buyers: Their Attitudes and Impact on Pre-Recorded Music Sales" (Fall 1980) ("CBS Survey"); and Roper Organization, Inc., "A Study on Tape Recording Practices Among The General Public" (June 1979) (conducted for National Music Publishers Association and Recording Industry Association of America) ("Roper Survey").

- When people do tape prerecorded music, they do so to get customized selection tapes or features, such as portability, quality, and convenience, that the recording industry has not made available in the marketplace.
- Tapers do not make recordings primarily to avoid purchasing records and prerecorded tapes.
- Active home music tapers are, by far, the most avid fans and heaviest buyers of prerecorded music.

1. Most Home Taping Does Not Involve Prerecorded Music

More than half of all home audio taping is done for some purpose other than taping prerecorded music.[11] In fact, a quarter of all home tapers never even tape prerecorded music.[12]

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[11] Specifically, "home tapers" (persons who made a home audio recording of any kind in the last two years) recorded something other than prerecorded music on 52% of the tapes they made in the three months preceding the Yankelovich Survey. Yankelovich Survey at 14, 36. In other words, fewer than half of the total tapes recorded at home contain prerecorded music.

[12] Yankelovich Survey at 15, 29. As well, 44% of tapers age 50 and over have never taped any prerecorded music. Yankelovich Survey at 15, 42-43. A study commissioned by the Copyright Royalty Tribunal confirmed that over half of home tapers (57%) do not tape music at all. *See* Wm. R. Hamilton, "A Survey Of Households With Tape Playback Equipment," at 5 (Sept. 1979) ("Hamilton Survey").

Tapers use audio recorders for a myriad of reasons, including family, educational,[13] and business purposes. For example, almost half of all home tapers surveyed record music performed by themselves or their family or friends, such as a child's musical recital or an amateur rock band.[14] Audio taping is a common element of both traditional festivities, such as weddings and birthday parties, and new technologies, from telephone answering machines to home computers.[15]

Beyond taping in the home, however, there is a plethora of uses for audio recorders that do not involve copyrighted prerecorded music. For example, over a half-million dictation machines are sold annually in the United States.[16] Private and governmental reporting services account for enormous numbers of recorders used in courtrooms, at depositions, and at congressional hearings.[17] Educational institutions use thousands of tape recorders -- in language labs or to tape music rehearsals. Non-profit institutions use recorders to bring literature, current events, and educational materials to the visually impaired, home-bound, or senior citizen communities.

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[13] Forty-five percent (45%) of home tapers tape for educational purposes, such as lectures. Yankelovich Survey at 14, 37-38.

[14] _Id_.

[15] _Id_. More than eight out of ten home tapers (82%) have recorded something other than prerecorded music. Yankelovich Survey at 37.

[16] _See_ Computer and Business Equipment Software and Telecommunications Industry 1960-1995, Industry Characteristics Report (1986).

2. Home Taping Does Not Compete With Prerecorded Music

The argument of the recording industry -- that it loses sales due to home taping -- is significantly undercut by the finding that when home tapers do record prerecorded music, the tapes they make are a very different product from the records and prerecorded tapes that are available in the market. For the great majority of tapers, home taping is largely a means of enjoying and organizing their music collections, not an alternative to or substitute for buying prerecorded music.

a. Home Tapers Tape Primarily To Put Together Their Own Program Of Selections

Tapers' primary reason for taping prerecorded music is to create their own programs of musical selections. More than seven out of ten home tapers rated "the ability to put together their own program of selections" as a "very important" advantage to home-recorded tapes as compared to both records and prerecorded tapes.[18] Tapers' actions confirmed their words: two-thirds (65%) of the average home tapers' collection of home-recorded tapes contained only musical selections, rather than complete albums.[19]

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[17] Assuming that each of the 18,000 members of the National Shorthand Reporter Association transcribed forty hours a week, they would, alone, account for thirty-six million hours of taping of noncopyrighted material on an annual basis.

Simply stated, the great majority of home-made tapes do not displace sales of prerecorded music because they are not duplicates of or substitutes for any pre-existing records or tapes. They are unique creations assembled by the taper, frequently from the taper's own collection of records and prerecorded tapes. For music lovers who are avid home tapers, selection taping is an opportunity to pursue their interest in music; it creates increased demand for purchasing and owning even more records and prerecorded tapes from which to excerpt selections.

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[18] This was, by far, the reason most often cited for preferring home-recorded tapes to prerecorded tapes. Yankelovich Survey at 17, 63-68. The CBS Survey confirmed that 75% of blank tape buyers use recording equipment to make "custom" tapes. CBS Survey at 11.

[19] Yankelovich Survey at 17. According to the Warner Survey, respondents spent over half (56%) of their time taping making recordings of selections. Warner Survey at 15.

b. Tapers Also Seek Portability, Convenience, Quality, And Availability Through Home Taping

Portability is another major reason for home audio taping. Tapers want music they can take where records will not go. Fully 75% of tapers cite portability, and 57% cite convenience, as "very important" reasons for sometimes using home-recorded tapes instead of records.[20] Tapers' emphasis on portability is understandable, because 80% of all home tapers own one or more portable tape players, such as car stereo systems or Walkman-type players. Until recently, the industry had been quite slow to offer or to promote portable music on high-quality prerecorded tapes, despite enormous growth in portable playing devices.[21]

Even when the demand for portability is met by prerecorded tapes, however, the tapes on the market have not satisfied the needs of home tapers. Over half (51%) of home tapers consider the longer playing time of home-recorded tapes a very important reason for preferring them to prerecorded tapes.[22] The better quality and greater durability of home-recorded tapes are also important to home tapers.[23] Furthermore, a third of tapers complain of limited tape availability (32%), and almost a quarter (21%) of home tapers reported that the stocking and selling practices of music stores make it difficult for them to buy those tapes that do exist.[24] A much greater understanding of the real reason for home taping is revealed by the fact that recording industry problems with the quality and availability of prerecorded tapes are considered most serious by those who do the most home taping of music.[25] Consumers, then, choose to

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[20] Yankelovich Survey at 18, 69-76. Over a quarter of those who tape albums most often do so to make copies of records for listening in their cars or offices. Warner Survey at 16.

[21] See infra Section IV.B.1.

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22 Yankelovich Survey at 19, 87-95.

23 Id.

24 Yankelovich Survey at 89-90. Seven percent (7%) of tapers in the Warner Survey gave the unavailability of prerecorded tapes as the single reason they most often made a home music tape. Warner Survey at 17.

25 For example, 58% of heavy tapers, as compared to 46% of light tapers, described as "very important" the longer playing time of home-recorded as compared to prerecorded tapes. The fact that some albums "are not available on prerecorded tape" was deemed a "very important" reason for preferring home-recorded to prerecorded tapes by 38% of heavy tapers, as compared with 28% of light tapers. Also, 36% of heavy tapers, as compared with 26% of light tapers, cited as "very important" the greater durability of home-recorded as compared to prerecorded tapes. Yankelovich Survey at 95.

tape at home because the recording industry has failed to provide prerecorded music in the form demanded by consumers.

c. People Do Not Tape Just To Save Money

Saving money is not the principal motivation for home taping -- notwithstanding the bald claims of the recording industry. Home tapers record primarily to obtain products or characteristics not otherwise available: tapes of customized selections, portability, and better quality. They do not tape only to avoid paying for records and prerecorded tapes.

Even when comparing home-recorded to prerecorded tapes, tapers do not list cost as the primary reason for making their own tapes. That is, virtually all tapers (99%) who mentioned cost also listed other reasons for preferring home-recorded tapes to records or prerecorded tapes.[26] Obviously, it is not surprising that most people do mention cost as a factor in home taping. The extent to which so many other factors are important in the decision to tape at home demonstrates clearly that home taping behavior does not simply displace sales of prerecorded music.

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[26] Yankelovich Survey at 21, 91-93.

d. Half Of All Home Tapes Of Prerecorded Music Are Made From The Taper's Own Records Or Tapes

Just over half (51%) of all music tapes made at home were made from the taper's own collection of records and prerecorded tapes.[27] Two out of three (66%) home music tapers had made home-recorded tapes from their own collection in the past six months.[28] The Warner Survey found that a similar share -- 45% -- of home music tapes are made from records and tapes in the taper's own collection.[29] Thus, recording from one's own collection is a major aspect of home taping and a significant factor in generating demand for the purchase of prerecorded music.

3. Home Audio Taping Stimulates Purchases Of Prerecorded Music

Probably the most important finding of these studies is that home taping often stimulates purchases of records and prerecorded tapes. In evaluating any proposal for an audio royalty tax, it is critical to assess the overall impact of home taping behavior and technologies on the recording industry. In particular, policymakers should recognize that taping prompts, rather than substitutes for, sales of prerecorded music. Thus, the tax proponents' charge that home taping represents lost sales of prerecorded music is belied by the surveys, which consistently show that home audio taping and music buying are complementary activities.

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[27] Yankelovich Survey at 22, 54.

[28] _Id_. at 22, 52.

[29] Warner Survey at 22.

The survey data dramatize this finding. The majority of home tapers (55%) often or sometimes buy a record after they have made a home tape of the whole record or selected songs or portions of it.[30] Home taping is thus a significant factor in promoting sales of prerecorded music.

The ability to tape stimulates the purchase of prerecorded music; many people buy records and compact discs just so they can tape them for their car, their personal stereo, or their office. That this is the common pattern of home taping behavior is confirmed by the fact that over half of all home music tapes are made from a taper's own collection.[31] For the home taper, a key component of the value of the purchase price is that the prerecorded music can be taped; by taping, the consumer can both preserve the music purchased, to prolong the period during which the music can be enjoyed, and expand the area in which it can be played.

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[30] Yankelovich Survey at 16, 45-48. Home taping of borrowed records has introduced two out of three tapers (64%) to musical artists or composers whom they discover that they like, and well over half (57%) have been prompted to buy records or prerecorded tapes after taping an artist's work. Id.

If, then, home tapers are deprived of their ability to tape -- or are subject to economic constraints when they do so -- the prerecorded music they desire to purchase will be less valuable to them. Thus, the economic consequence of the symbiosis between record purchases and home taping is clear: Tapers view their ability to tape prerecorded music as an important component of the price they pay. If they were not able to make recordings from their collections -- or were taxed for doing so -- they will be less likely to want to buy prerecorded music.

Buying prerecorded music and home audio taping are complementary activities arising from a common source. The Warner Survey concludes that,

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[31] Yankelovich Survey at 22, 49, 58. The recording industry's surveys confirm that home tapers "tape primarily from their own collections." Roper Survey at 3 (tapers' own record and tape collections are "the largest single source" of home recordings); CBS Survey at 12 (40% from own collection).

> buying and taping both reflect a more general commitment to music. That is, the more one sees music as important, the more likely one is to engage in both buying and taping.[32]

This general commitment to music manifests itself in a variety of attitudes and behavior. Home audio tapers who buy prerecorded music are much more likely than persons who buy but do not tape music to rate music as a "very important" element in their lives.[33] Interest in buying music, records, and prerecorded tapes, and home taping reinforce each other, with each behavior building on and gaining momentum from the others.[34] Home taping and buying prerecorded music apparently go hand-in-hand.

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[32] Warner Survey at 36.

[33] Warner Survey at 33, 35. Those who both tape and buy prerecorded music are more likely than others to rate themselves as knowledgeable sources of information about prerecorded music (38% affirmative for taper-buyers compared to 20% for tapers-only/18% for buyers-only), are more likely to "consider themselves collectors" (51% for tapers versus 17% for non-tapers), and to discuss prerecorded music with others (38% versus 6% of non-tapers/non-buyers). Warner Survey at 36-39. Tapers are also substantially more likely than non-tapers to go to live concerts (55% compared to 30%), to read about music (62% versus 36%), and to prefer receiving records and tapes to other items as gifts (74% versus 40%). Warner Survey at 39.

[34] Interestingly, heavy radio listeners, who might be expected to tape music from the radio instead of buying prerecorded music, are in fact more likely than lighter radio listeners to buy prerecorded music cassettes, by margins of 8%-49% above the average, depending on age. McGavran-Guild Research, "Cassette Tapes, Radio and You" (1982). Once again, music listening and buying appear to be additive rather than substitute behaviors.

The heaviest home music tapers illustrate this point most dramatically. Those who tape the most prerecorded music, on average, are also the largest purchasers of prerecorded music. According to the Roper Survey,

> Based on reports from all adults, those who record music on tape are much heavier buyers for their own use of records, pre-recorded tapes and blank tapes than are non-recorders . . . .
>
> Roughly twice as many adult tape recorders as non-recorders buy LP records, singles and pre-recorded 8-track tapes. Four times as many recorders as non-recorders buy pre-recorded cassettes . . . .[35]

Moreover, tapers spend much more money than non-tapers on prerecorded music.[36] For these most active home tapers, there is a complex synergistic relationship between buying prerecorded music and home audio taping. It is not important where the cycle begins, whether buyers tape at home to maximize enjoyment of their prerecorded music, or whether they buy more prerecorded music because they can tape it. What is important is that prerecorded music buying and taping together represent a continuous cycle rather than alternative behaviors. As Arthur H. White, Vice President of Yankelovich, Skelly and White, put it in his testimony before the Subcommittee on Courts, Civil Liberties, and the Administration of Justice of the House Judiciary Committee, "In short, those who tape also buy, and the more they tape, the more they buy."[37]

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[35] Roper Survey at 6-7. Indeed, eight out of ten (82%) of the tapers surveyed were current buyers of records and prerecorded tapes, while only 44% of non-tapers reported purchasing prerecorded music. Warner Survey at 32. According to the CBS Survey, 80% of blank tape buyers also purchase prerecorded music. CBS Survey at 6.

[36] Although only 31% of record and prerecorded tape buyers are tapers, in dollar terms they account for almost half (48%) of the total amount spent on prerecorded music. Warner Survey at 32. Heavy tapers own approximately three times as many record albums and prerecorded tapes as light tapers. Yankelovich Survey at 16, 61-62.

It is obvious from these findings that a royalty would unfairly penalize home audio tapers, and particularly the most active home music tapers, who are the lifeblood of the prerecorded music industry. Home taping, especially among heavy tapers, stimulates the purchase of records and tapes by increasing interest in and demand for prerecorded music. Imposing royalty taxes on sales of audio recording equipment and blank tapes would endanger this delicate relationship. Summing up the irony of the industry's all-out assault on home tapers, Rolling Stone magazine said

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[37] *Home Recording of Copyrighted Works: Hearings on H.R. 4783, H.R. 4794, H.R. 4808, H.R. 5250, H.R. 5488, and H.R. 5705 Before the Subcomm. on Courts, Civil Liberties, and the Administration of Justice of the House Comm. on the Judiciary*, 97th Cong., 2d Sess. 1040 (1982) (statement of Arthur H. White).

> Home tapers aren't a bunch of freeloaders, they're the very people the record industry depends on to turn a release platinum . . . . In essence, the record industry is saying that its best customers are its worst enemies.[38]

4. Recording Technology Contributes Significantly To The Recording Industry

Without the development, marketing, and widespread consumer demand for and acceptance of recording technologies, the industry would still be left to exploit live, over-the-air, and "black vinyl" renditions of sound recordings. It is only with the invention and distribution of recording devices that the recording industry has been able to sell prerecorded tapes or records that are bought to be taped.

Its campaign to depict technology as the enemy of the creative community -- a characterization most visible in the anti-technology bias inherent in the royalty tax proposals -- defies logic and economic reality. The facts show that home taping technology has created a multi-million, if not billion dollar, annual prerecorded tape market for the industry. Many key retailer and record company executives do recognize the valuable contribution that home recording technology has made to their industry. As Russ Solomon, President of Tower Records, said in a recent interview:

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[38] "The War Against Home Taping," Rolling Stone, Sept. 16, 1982, at 59, 64.

> [I]f you didn't have the home-recording business, you wouldn't have Walkman machines. In other words, the tape technology that came out of the recording machine resulted in the portable playback machine and the automobile machine, which created an enormous market for us.[39]

5. The Recording Industry Surveys Fail To Prove That Home Taping Has An Adverse Impact On Copyright Owners

The recording industry acknowledges that consumers and manufacturers of audio recording equipment and tape can only be asked to pay for sales "lost" as a direct result of home taping.[40] To support its claim that sales are displaced by home taping and that the impact of such behavior on the industry is negative, the recording industry has rested on two studies -- the Warner Survey of 1982 and that undertaken by Audits & Surveys in 1983 -- and two analyses by Dr. Alan Greenspan based on the data from those surveys.[41] The studies and analyses, however, 1) ignore entirely the stimulative impact of home taping behavior on the purchasing of prerecorded music; 2) disregard the benefits to copyright owners and the entire creative community from the recording technology that the industry seeks to tax; 3) assume that taping is a substitute for the purchase of prerecorded music when the data demonstrate that it is not; and 4) are so riddled by methodological and analytic errors as to be completely unreliable as a basis upon which Congress can or should determine to burden home tapers.

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[39] M. Goldberg, "The Wisdom of Solomon," Rolling Stone, Nov. 22, 1984, at 39.

Russ Solomon's words echo those of Jan Timmer, now president of PolyGram International, who commented on home taping technology at the International Music Industry Conference in 1982:

> [Y]ou can't have the blessings of technology without trying to cope also with the unpleasant aspects. I would, however, suggest that the influence of technology has been positive and stimulating and the negative aspects, which we all recognize, are not of greater importance than the beneficial elements.

"IMIC '82: The Challenge of Change: Timmer Keys on New Technology," Billboard, June 5, 1982, at 53.

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[40] See "Audio Home Taping: The Case for a Fair Deal for Copyright Owners and Consumers," at 2-6, 16-22, reprinted in Hearings on S. 1758, supra note 5, at 712-16, 725-31.

[41] See Hearings on S. 1758, supra note 5, at 920 (statement of Dr. Alan Greenspan); Video and Audio Home Taping: Hearings on S. 31 and S. 175 Before the Subcomm. on Patents, Copyrights and Trademarks of the Senate Comm. on the Judiciary, 98th Cong., 1st Sess. 229 (1983) (statement of Dr. Alan Greenspan) [hereinafter "Video and Audio Home Taping"].

a. The Net Effect Of Home Taping On The Recording Industry Is Beneficial, Not Harmful

As described above,[42] home taping has a stimulative effect on the sales of prerecorded music. An important aspect of the value of purchased music is that it can be taped. Listeners also buy music after being exposed to artists and performers on home-recorded tapes. With its tunnel vision on the purported evils of home taping, the industry never looks at the whole home taping picture -- made up of allegedly displaced sales and the substantial sales that are stimulated by the availability of home taping. Thus, neither the industry nor Dr. Greenspan even tries to measure the net impact of home taping.[43]

In its crusade against home taping, the industry also refuses to credit taping technology for developing multi-billion dollar markets for prerecorded music and, thereby, making extraordinary contributions both to artists' livelihoods and to record company bottom lines. As discussed above,[44] rather than fearing recording technologies, the industry should recognize that they are among its greatest friends. Thus, although the industry surveys aim high, they fall well short of the mark because they do not even attempt to tell the entire home taping story. They focus narrowly on the allegedly detrimental impact of home taping, while never once conceding that recording technology has poured billions into record company coffers -- without the industry having to lift even a finger.

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[42] See supra Section III.A.3. (discussing the stimulative impact of home taping).

[43] In neither his April 1982 nor his October 1983 testimony, does Dr. Greenspan integrate the stimulative effect of the ability to tape prerecorded music into his analysis. Although Audits & Surveys did attempt to ascertain whether home taping stimulates record purchases, it asked the wrong questions: asking why people bought a record does not adequately probe the symbiotic behavior of purchasing and taping prerecorded music.

Moreover, the industry's argument that home taping displaces sales of prerecorded music depends on the presupposition that home taping substitutes for music that is available for purchase. Given, however, what is known about what and why people tape at home, as described above, that assumption, fundamental to the industry's case, cannot withstand scrutiny.

The industry relies on the analyses of Dr. Greenspan to support its contention that home taping has a negative impact on sales of records and prerecorded tapes. Dr. Greenspan asserts that "home taping should be viewed as an alternate means of acquiring recorded music."[45] With this bias, he then estimates that more than two-fifths of home taping was in lieu of the purchase of prerecorded music in 1982.[46] This estimate is credible only if records and prerecorded tapes are, in fact, close substitutes for tapes recorded at home. As has been discussed in some detail, they are not.[47]

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[44] See supra Section III.A.4. (discussing contributions of technology to the recording industry).

Where the industry position is flawed initially, then, is in its failure to exclude from the total of sales purportedly lost from home taping all home taping that is not -- indeed, could not be -- a substitute for prerecorded music, i.e., home taping that provides something that is not available in the market. Further, the industry surveys and Dr. Greenspan's analysis do not appropriately discount all taping done from one's own collection of records and prerecorded tapes: this music has already been bought and paid for.[48]

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[45] Video and Audio Home Taping, supra note 41, at 226.

[46] Id. at 86, 229.

[47] In seeking a preliminary injunction against a proposed joint venture involving Warner Communications Inc. and Polygram Records, Inc., the Federal Trade Commission argued that the recording industry exaggerates the amount of home taping and that consumers do not view home taping as a substitute for prerecorded music. See "Merger of Warner Unit, Polygram Angers Troubled Record Industry," Wall Street Journal, Apr. 12, 1984, at 33. The Ninth Circuit Court of Appeals, in issuing the injunction, noted the distinct characteristics of prerecorded music and held that "prerecorded music and home tapes are not interchangeable." F.T.C. v. Warner Communications Inc., 742 F.2d 1156, 1163 (9th Cir. 1984).

In sum, the recording industry grossly overstates the extent to which home taping is harmful because it relies on the unsupported assumption that home taping substitutes for the purchase of prerecorded music. When this defect in the industry's case is, however, combined with the stimulative effect of home taping, and the ample and well-documented benefits of recording technology, nothing is left from which the industry is able to demonstrate -- or Congress could conclude -- that the net impact of home taping in any way warrants extracting yet more compensation from the American public.

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[48] Thus, for example, when a home taper records his or her favorite symphony for a car stereo because it is not available on tape, it is obvious that no tape sale is displaced. Audits & Surveys attempted to compel respondents to state that they would have bought another, albeit less satisfying, tape in lieu of taping. Although the Audits & Surveys report and Dr. Greenspan attempted to extrapolate from the data to conclude that this hypothetical purchase represented a lost sale, the methodology and approach of the recording industry surveys have been far too crude to measure the extent to which such speculative responses represent actual displacement.

b. The Industry Surveys And Dr. Greenspan's Analyses Overstate The Amount Both Of Home Taping And Of Displaced Sales And Are So Rife With Methodological Flaws That Congress Cannot Rely Upon Them

While oblivious to the true nature of home taping, and to its stimulative and beneficial impact on copyright owners, the industry surveys and Dr. Greenspan have attempted to gather and analyze some data to tell their side of the story. Under rigorous examination, however, the evidence of harm that they proffer is revealed to be so defective as to be of no probative value for decisionmakers.

As a preliminary matter, the industry surveys do not even address the various uses to which tape recorders are put by businesses or educational institutions -- as distinguished from taping at home -- such as dictation and the taping of telephone conversations, conferences, interviews, training programs, and hospital operating room discussions.[49] Thus, the surveys consistently misstate the impact of home music taping by greatly exaggerating both the actual amount and its proportion to overall audio taping. This distortion is particularly troubling because the industry is attempting to persuade Congress to impose a tax on all audio recorders.

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[49] A very substantial percentage of the audio recorders sold in the U.S. is consumed by businesses. Many businesses, particularly small-scale businesses, purchase recording equipment from ordinary retail stores. Consequently, hardware destined for business use cannot be distinguished from that destined for home use.

As significant, the estimates of home audio taping are based on data that are grossly defective. First, the industry's own estimates of sales lost due to home taping have fluctuated dramatically over the years and are, at best, woefully uncertain.[50] Moreover, the industry is asking decisionmakers to believe the incredible -- that the number of albums of music taped in a survey year is substantially in excess of the known amount of tape sold in that year. The Audits & Surveys estimate of home music taping is two to three times larger than the amount of tape sold.[51]

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[50] In 1982, Dr. Greenspan estimated that lost record sales in 1981 were approximately $900 million. Hearings on S. 1758, supra note 5, at 920. Based on the Audits & Surveys data, he opined only a year later that losses had risen by over 55%, to over $1.4 billion. See Video and Audio Home Taping, supra note 41, at 229. The Warner Survey, using 1980 data, estimated lost sales at between $609 million and $2.85 billion annually. Warner Survey at 46.

[51] See Video and Audio Home Taping, supra note 41, at 419, 420-21 (statement of Nina W. Cornell, President, Cornell, Pelcovits & Brenner) Dr. Cornell's estimate is based on the number of blank tapes sold in 1982, as reported by the International Tape Association, on the assumption that each blank tape can hold 75 minutes of material, and on the recording industry's determination that each album is 45 minutes long. She concludes, using the Audits & Surveys estimate of home

Furthermore, the industry calculations do not even take into account the substantial quantity of cassettes sold to businesses for taping other than copyrighted music. If the recording industry surveys had taken this number into account, there would be an even more striking disparity between the tapes actually sold and the amount of music that the industry claims is taped at home.[52]

The overstatement of the amount of home taping is not merely of academic significance, for it strikes at the very core of the industry's contention that home

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[footnote continued]

music taping, that that estimate exceeds blank tape sales by 180%. Using the findings of the Yankelovich Survey, the Audits & Surveys estimate exceeds sales of blank tape by 310%. The Warner estimates of cassette purchases exceed actual factory sales of cassettes by 18% when compared with the figures for the "60th Annual Statistical and Marketing Report" in the March 1982 Merchandising Magazine. The Merchandising Magazine figure is an average of 1979 and 1980 data, and the Warner Survey data is for the twelve months ending June 1980.

[52] It is, of course, possible to re-record on audio tape. Nevertheless, this practice means that many tapes are kept for only a short time. Buried in a footnote in Dr. Greenspan's analysis is the notation that his estimates of displacement are based on a single use of a blank tape purchased in 1982. Video and Audio Home Taping, supra note 41, at 90 (Table 5, note 1). Of course, if tapes are erased and used more than once, as seems likely, it would be difficult for Dr. Greenspan and the recording industry to assume, as they do, that taping displaces, or substitutes, for purchase.

taping harms copyright owners. Relying on the Audits & Surveys data on the amount of home taping, Dr. Greenspan proceeded to derive his estimates of displacement of sales of prerecorded music.[53] Thus, as the volume of home taping is too large, so, too, are the estimates of lost sales.

In addition to the exaggeration in the estimates of the amount of home taping, the estimates of displaced sales, which are based on the Audits & Surveys data, are also inflated as a result of the serious methodological flaws in the survey procedure used. First, the methodology violated a basic principle of market research: it asked people to make hypothetical buying decisions by asking whether they would have bought a record or prerecorded tape had they not been able to make a tape and, if so, how many they would have bought had they not been able to tape. It is impossible to obtain reliable data from questions that call for entirely speculative responses. People will always say that they are more willing to spend money than they are actually to spend it.[54]

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[53] Id.

[54] Asking a respondent who tapes a record that he or she already owns how many copies would have been purchased had taping not been possible, invites respondents to say that they would have bought one or two or more additional copies of a record already in their

A second problem with the Audits & Surveys approach to estimating lost sales is that it invited respondents to say that they would have purchased an album of a tape for which no album either was available or could, in fact, have been purchased. Home recorded tapes of customized selections, or tapes of a live concert, are not readily available commercially.[55]

Third, Audits & Surveys also asked people how many records or prerecorded tapes they would have purchased had they been unable to tape. It is incredible that people would have bought multiple copies of the same recording if they could not have made their own tape. To count each of these multiple copies as a displaced sale is to demonstrate further the exaggeration of the estimate of lost revenues from home taping.

[footnote continued]

collections. Such questions -- and responses -- defy common sense.

[55] Thus, Audits & Surveys invited unreliable responses. According to its report, 40% of all music tapes are made from radio, concerts, and from home-recorded tapes. Audits & Surveys at 9. As many of such tapes are not available, or have some special value to the taper, 40% of the decisions respondents were invited to make were purely speculative, with no grounding in commercial reality.

A fourth problem with the methodology was that it presupposed that individuals would buy an entire album even though they only taped a selection from that album. Audits & Surveys counted each "selection" taped as a lost album sale.[56] And, from the information available, it appears that a third of the total estimate of displacement is from respondents who said they would have done just that.

Fifth, the survey report of the RIAA releases no data on how many tapes were made from a respondent's own collection. Given the improbability that tapers would have bought a second copy of music already in their collections, Dr. Greenspan nevertheless estimates that 42% of taping from records already owned by a taper would have resulted in purchases of additional copies.[57] From this, and other data, he derives his over-estimates of sales displaced by home taping behavior.

Aside from the statistical flaws with respect to both the amount of home taping and estimates of displacement based thereon, a major underlying methodological difficulty with the Audits & Surveys approach is the novel manner in which the data were collected, through in-home visits. The validity of the data gathered with respect to home taping depends entirely on whether the interviewer asked for -- and was shown -- home recorded tapes containing other than prerecorded music. There is no indication that each and every type of home recorded tape was produced, wherever located in the home. The interviewer asked only about "home recorded tapes," not reminding the respondents of the wide range of possible uses in addition to taping music; nor is there any suggestion that the interviewer asked about locations where non-music tapes might be found.

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[56] Audits & Surveys at 29.

[57] Video and Audio Home Taping, supra note 41, at 228-29 (statement of Dr. Alan Greenspan).

Moreover, the weekly telephone surveys used by Audits & Surveys also were designed to produce results that overstated the amount of home music taping. The questions asked focused on the taping of music; it is quite possible, therefore, that subsequent interviews with telephone respondents were with individuals who recorded music.

Similarly, it is not surprising that Audits & Surveys did not obtain accurate information with respect to the stimulative effect of home taping on record purchases. Respondents were not asked whether they bought records to make them portable, to preserve them, or to make selection tapes. Thus, the estimate of displacement overstates the impact of taping on the purchases of prerecorded music.

That the Audits & Surveys statistics are imprecise is acknowledged openly by the report, which concedes that the data collected could be interpreted to arrive at an entirely different breakdown between copyrighted and noncopyrighted material -- 65% to 35%, when measured by the total amount of taping, in contrast to 84% to 16%, as derived by the audit approach taken.[58] Although the report speculates as to the difference between these two breakdowns, there is no reason to do so. The data were collected -- the recording industry refuses to release them.[59] How credible, then, is the industry's own survey, when its statistics demonstrate that the taping of copyrighted music can vary by almost 20%?

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[58] Audits & Surveys at 10.

[59] The failure to release certain critical information makes the Audits & Surveys report entirely inadequate as a basis for important public policy determinations. For example, even though the survey inquired as to the ownership of records that were recorded by home tapers -- whether owned by the taping household or by someone outside that household -- the results have never been released. Nevertheless, answers to that question are crucial, both for determining whether people would have bought a record had they not been able to tape it and as to the equity of any proposal to penalize each of the various home taping practices. See infra Section III.B.

In short, the data collected by the recording industry surveys simply do not provide a complete picture of home taping. The statistics that are proffered by the industry are far from complete; they are flawed, and rife with methodological anomalies, if not defects. Dr. Greenspan's analyses, which are based on the industry data, cannot help, then, but be inaccurate. Industry claims of damage remain, therefore, undocumented. To summarize, a royalty tax is unjustified because there is no competent evidence that, on balance, sales of prerecorded music are hurt by audio taping.

B. Congress Must Determine Whether Each Type Of Home Taping Activity Should Be Penalized, Requiring Payment Of A Royalty To Record Companies

Given the nature and scope of home taping activities, and the failure of the recording industry to document its claims of harm, Congress must decide whether home taping should now be subject to legislative sanction. This determination requires, first, that there be an understanding of the policies underpinning the copyright law and, second, an application of those policies to the several different kinds of home taping behavior in which consumers engage. In particular, Congress must determine whether a new consumer tax, which would constitute double payment to record companies for use of prerecorded music, is consistent with the delicate balance between the interests of the public and the proprietors that is embodied in the copyright law.

1. The Recording Industry Claims Must Be Balanced With The Interests Of The Public

Congress must take into account the constitutional principles on which copyright law is based in reviewing the claims of the copyright owners that all home taping has an adverse economic effect for which compensation is owed. In formulating copyright policy, it is clear that proprietor interests ultimately serve, and must be balanced against, the cause of promoting the broadest public availability of creative endeavors. In 1984, the Supreme Court reaffirmed that the copyright law must balance competing claims of rewarding creativity and of serving the cause of wide dissemination of such creative work. In Sony Corp. v. Universal City Studios, the Court acknowledged that the "immediate effect of our copyright law is to secure a fair return for an 'author's' creative labor" but reemphasized that "the ultimate aim is, by this incentive, to stimulate artistic creativity for the general public good." 104 S. Ct. 774, 783 (1984), quoting Twentieth Century Music Corp. v. Aiken, 422 U.S. 151, 156 (1975).

Hence, the copyright scheme is neither intended nor designed to guarantee a profit or a subsidy for the recording industry or to secure preferential treatment of any particular medium or industry over another. Rather, it recognizes the interests of the public and relies upon the marketplace to balance the rights of copyright owners and the citizenry. By forcing consumers to pay a new, federally-legislated, royalty tax, the recording industry proposals depart dramatically from the sound principle that copyright owners are to find appropriate incentives for their creative work in marketplace mechanisms.[60]

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[60] The current Copyright Act only provides for four areas where copyright compensation is set by law:

1. Secondary Transmissions by Cable Systems, 17 U.S.C. § 111 (rebroadcast of tv signals by cable tv systems);
2. Making and Distributing Phonorecords, 17 U.S.C. § 115 (covers organizations that are unable to locate the name and address of a copyright owner for the purpose of compensating the owner, or if the owner is unwilling to negotiate);
3. Public Performances on Coin-Operated Phonorecord Players, 17 U.S.C. § 116 (jukeboxes); and
4. Use of Certain Works in Connection with Noncommercial Broadcasting, 17 U.S.C. § 118 (covers negotiations between entities such as the Public Broadcasting System (PBS) and groups that represent copyright owners, such as the

At present, the copyright law strikes the appropriate balance by affording copyright owners the exclusive right to reproduce their works. Congress created this right to permit proprietors to control -- and reap the profits from -- commercial reproduction and distribution. By exercising that right, copyright owners enjoy a monopoly, for a limited period of time, over commercial use; the right excludes others from competing with the copyright owner in the publication of the material.

Enactment of royalty tax legislation, however, would essentially enlarge the proprietor's right of reproduction to cover noncommercial taping by consumers. Not only would such an expansion tilt unduly the constitutional balance struck in the 1971 Act, but it would also afford copyright owners unprecedented rights with respect to noncommercial users.

[footnote continued]

American Society of Composers, Authors, and Performers (ASCAP)).

Copyright Office, Circular R75 (1980).

These four categories involve specialized situations where copyrighted material is offered to others, in most cases on a commercial basis; the royalty is payable by those who operate these services and not by the supplier of the devices used in providing the services.

That is, for commercial users, reproduction is an act of economic significance. When it granted owners of copyrights in sound recordings the exclusive right to authorize commercial reproduction, Congress recognized this fact.[61]

Unlike commercial reproduction, however, home taping is, for the ultimate consumer, simply one way of enjoying music after the chain of exploitation has run its course. Home tapers do not "publish" (*i.e.*, couple reproduction and commercial distribution) the music that they have taped. Their activity is different in kind from that of commercial users because it has no independent economic significance. Therefore, Congress would distort the balance between the interests of the public and proprietors if it were to broaden the present rights of copyright owners to include exclusive control of some noncommercial uses.

2. The Royalty Tax Constitutes Double Payment To Copyright Owners

Given the balancing of interests inherent in the copyright law, the existing limited scope of the reproduction right, and taking into account the true nature of home taping,[62] it is evident that the recording industry proposals would extract from home tapers an unwarranted double payment for the use of prerecorded music. Home taping is not, as the recording industry attempts to depict it, akin to theft. When people buy prerecorded music they are not simply purchasing a piece of vinyl or some magnetic tape in a shell. Rather, they are, quite clearly, purchasing the right to enjoy the music. When they tape that music, whether for listening in their car, on their portable stereo, or at the office, they are doing no more than extending the area in which they can enjoy what they have bought.

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[61] *See supra* Section II.

Viewed correctly, then, much home taping activity is simply an enhancement of prerecorded music for which the consumer has already paid the copyright owner. Thus, unless the recording industry is contending that music can only be enjoyed by the purchaser in one location and at one time, the proposed tax on home tapers would double the compensation to copyright owners.

In striking the copyright balance, which was expressly reaffirmed in the Sony decision, no such double payment can be justified. The payment of a royalty goes far beyond what the recording industry attempts to characterize as "compensation." The levy would require that part of the price that consumers pay for audio recording equipment be paid over to the recording industry. Although the royalty tax would purport to generate payment for the use of copyrighted materials, in fact it utterly disregards the actual price of such copyrighted material in the marketplace. Hence, Congress must determine whether the economic impact of the various types of home taping justifies imposing what is a stiff and arbitrary royalty tax on millions of American consumers.

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[62] See supra Section III.A.

3. No Royalty Is Warranted Because The Great Majority Of Home Taping Has No Adverse Impact On Copyright Owners

In measuring the recording industry proposals against the policies underlying the copyright law, Congress should recognize that much home taping activity in no way harms the recording industry. The analysis that it should follow requires a careful examination of the kinds of home taping and an understanding of how home tapers behave. First, in determining whether a levy should be placed on recorders, it is essential to recognize that an extremely high percentage of the recordings made at home are not of prerecorded material.[63] Thus, the principal impact of a royalty would be on uses other than the uses -- of prerecorded music -- for which the recording industry expresses concern.

Even as to taping of music, taping behavior is not undifferentiated. Tapers record off their own records and tapes, off radio broadcasts, and off borrowed material. There are different reasons why tapers engage in each of these taping activities and, consequently, each type has different economic consequences. Because the proposed royalty scheme will not and, indeed, cannot distinguish between the varied uses to which consumers put their recorders, Congress must reach the conclusion that all taping activity -- from whatever source -- should be made illegal before it adopts the scheme advocated by the recording industry.

a. Taping Off One's Own Records And Tapes

Should taping off one's own records and tapes be an infringement of copyright? As discussed above, the most common taping practice is the taping of prerecorded music from a taper's own collection.[64] People tape to enhance their enjoyment of the music they own and they do so for many reasons: to preserve records, for ease of use and longer playing time, to listen on car stereos and portable stereo sets such as the Walkman, and to put together a home-recorded music tape composed of selections chosen by the taper.[65] Taping for these purposes is entirely legitimate and must be viewed by Congress as unobjectionable.

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[63] See Yankelovich Survey at 14, 36.

[64] See supra Section III.A.2.d.

Any proposal that seeks to tax people for taping music for which they have already paid either expects them to buy multiple copies of the same music or, in the case of selection taping, seeks to prevent them from making any customized compilations of material in their collections. It is improbable that Congress could strike the constitutional balance to prohibit -- or constrain economically -- activities that simply facilitate or expand the listener's enjoyment of the works that are already owned. One of the reasons for exempting home taping from copyright infringement in 1971 was that the practice was viewed as legitimate and widespread. Arguing now that home taping should be considered infringement because it has become even more common is, quite simply, illogical.

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[65] See Yankelovich Survey at 17-22, 57, 79, 89, 94.

b. Taping Off Radio Broadcasts

When Congress turns to the question of whether it should tax off-air taping, it must decide whether those who engage in such an activity, for private, noncommercial purposes, must pay when broadcasters, who clearly profit from their use and exploitation of sound recordings, pay nothing.[66] As noted earlier,[67] the protection afforded the owners of copyrights in sound recordings does not encompass the exclusive right of public performance. Accordingly, radio broadcast stations and others that make commercial use of recorded music do not pay any compensation to record companies for the use of their sound recordings. Congress has repeatedly rejected the idea of expanding copyright protection to afford the recording industry a legal basis for claiming compensation for these commercial uses.[68]

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[66] According to the findings of the Yankelovich Survey, only 21% of all music tapes made at home are made from off-the-air radio broadcasts. See Yankelovich Survey at 54. Audits & Surveys reported a slightly higher figure, 31%. See Audits & Surveys at 9.

[67] See supra note 3.

[68] It should be noted that radio stations often make tapes of programs, including music programs, for purposes of broadcasting, without rendering any compensation to the record companies.

Commercially-operated radio stations generate revenues from the sale of advertising time to sellers of goods and services. Consumers pay for these advertising costs through their purchases of those goods and services. Therefore, programs -- including music -- that are broadcast, and lawfully received are now paid for by consumers. Clearly, then, the reception and taping -- for private, noncommercial purposes -- of programs for which payment has already been made should not be subject to further payment. This would especially appear to be the case when commercial users are entirely free to exploit the same sound recordings, even by taping them for their commercial advantage.[69]

Finally, the statutory definition of "broadcasting," and interpretive glosses thereon, demonstrate that when broadcasters transmit programming they intend that it be received by all those in the general public who have the means to do so.[70] Off-air home taping of such programs should be regarded as one form of reception, with no more adverse economic effect, if any at all, than the repetition inherent in the multiple broadcasting of the programming itself. Such taping should not, therefore, be deemed an infringement or singled out for a special levy.

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[69] Congress continues, to this day, to refuse to expand the scope of protection under the copyright law to afford the owners of copyrights in sound recordings the exclusive right of public performance, despite the repeated efforts by the recording industry to obtain such protection. In other words, even with respect to entirely commercial uses, such as radio and television broadcasting, jukeboxes, dance clubs, and restaurants, Congress has not felt it appropriate to grant additional rights to such copyright owners.

c. Taping Off Borrowed Sources

When assessing the impact of taping prerecorded music borrowed, Congress should, at the threshold, consider whether ordinary and accepted human conduct -- the borrowing and lending of goods within a family or among friends -- should be burdened or restricted by legislation.[71] The balance between the copyright owners and the public historically has included the concept that once a copyright owner sells a copy of a work, that copy is then available for use by the public.[72]

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[70] The Communications Act defines "broadcasting" as "the dissemination of radio communications intended to be received by the public . . . ." 47 U.S.C. § 153(o)(1984). The Federal Communications Commission has defined a broadcast service as one where the broadcaster intends "to provide radio or television program service without discrimination to as many members of the general public as can be interested in the particular program . . . ." Further Notice in the Matter of Subscription Television Service, 3 F.C.C.2d 1, 9-10 (1966). See also National Ass'n of Broadcasters v. F.C.C., 740 F.2d 1190, 1201 (D.C. Cir. 1984) (test for broadcasting is whether there is "intent for public distribution" [emphasis in original]), quoting Functional Music Inc. v. F.C.C., 274 F.2d 543, 548 (D.C. Cir. 1958), cert. denied, 361 U.S. 813 (1959).

The copyright law recognizes, therefore, that the ability to share a copy of a copyrighted work is an important component of the purchaser's ownership right. Indeed, the common expectation is that a book, magazine, or newspaper, once purchased, can be passed around. Yet, there is no suggestion that there should be any economic restriction on the ability of friends to lend a favorite book to others.

Similarly, friends or family members naturally are inclined to want to share music that they enjoy. Many owners of prerecorded music, however, would prefer not to lend records in their collection because they want to ensure that their albums are handled properly. Thus, the way in which prerecorded music is shared is to tape the music on such albums for friends or relatives. There is no greater harm in this practice than there is in letting others read a book that one owns.

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[71] It is obvious that not everyone tapes from borrowed records; the Yankelovich Survey found that only 28% of home-recorded tapes were made from prerecorded, borrowed music. See Yankelovich Survey at 54. Before deciding to tax such taping activity, it is essential that the number of people who engage in it be measured objectively.

[72] This notion is codified in the "first sale" doctrine of the Copyright Act of 1976. 17 U.S.C. § 109(a) (1984). It has its roots in the 1909 copyright law and the tenet of Anglo-American jurisprudence that private property should be free from restraints on alienation.

Owners of musical works and sound recordings, however, now seek a new right -- to control a noncommercial use -- that is not available to those owning copyrights in literary or other kinds of works. The recording industry proposals would disrupt what has always been thought an unremarkable behavior of sharing. Congress should carefully consider whether conduct that is private, noncommercial, and essentially a normal part of social interaction, has such adverse economic consequences for some copyright owners as to warrant imposition of a royalty tax on all home taping activity.

In evaluating the impact on copyright owners of such taping among friends or within the family unit, Congress should weigh the following additional factors:

First, if only a portion of a borrowed album is taped, there exists a continuing opportunity to sell the same album to the taper whose interest in the album or the artist was stimulated by the exposure through borrowing. In general, home taping of borrowed material can be beneficial because sales of prerecorded music may be stimulated by the interchange of music among relatives or friends.[73]

Second, it is simply inaccurate to conclude that people who tape from borrowed material would have purchased the records or tapes if they were unable to make their own recordings. For, in many cases people prefer a tape format rather than a disk. Furthermore, by no means are all record titles available on prerecorded cassettes, or on high-quality tape. As well, many people tape only a portion of the album borrowed so as to make a customized tape of their favorite music, which, again, would not be available in the market. Finally, most consumers have a finite disposable income; thus, if taping were constrained economically or were impossible, it is improbable that those who tape would instead make an equivalent number of purchases of prerecorded music.

What is clear is that there is a wide range of home taping activity, all of which would be burdened by a royalty tax. The vast majority of home taping, however, is unobjectionable and has no economic effect on

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73 See supra Section III.A.3.

copyright owners. Taxing such taping would result in a financial windfall for record companies. For other kinds of taping, Congress should determine whether it should first force commercial users to pay befor taxing private, home taping activity. Yet other, less common, taping activities require that Congress apply the policies of the copyright law to weigh the costs of intruding on normal patterns of social behavior against the economic impact of such behavior on copyright owners.

IV. The Recording Industry Needs No Additional Compensation From Home Tapers

Over the last few years, the recording industry has insisted that a royalty tax on audio recorders and, until recently, tape is justified because sales of prerecorded music should have been higher and that home taping is responsible for the shortfall. The industry's record profits and sales in 1983, 1984, 1985, and, now, 1986 demonstrate what has been apparent for years: the industry simply uses home taping as a convenient scapegoat. The temporary downturn in the sales of prerecorded music can be explained by several factors -- the poor state of the economy, fierce competition from the video revolution, and significant marketing errors by the industry. Now, however, the industry is riding a boom. There is, therefore, no reason for Congress to give the industry the windfall that it seeks.

A. These Are The Recording Industry's Best Years Ever

The industry has enjoyed tremendous financial and artistic successes since 1982, even though Congress did not capitulate to its pleas with respect to home taping. In 1983, in 1984, in 1985, and in 1986 industry revenues have moved upward to all-time highs. In 1984, the industry had its best year ever, with revenues rising 15% to $4.37 billion, exceeding the previous record, set in 1978, of $4.13 billion.[74]

In 1984, virtually every record company had a banner year of profits and revenues. CBS Records Group led the way with an all-time high of $1.27 billion in sales, representing a 9% increase in revenues.[75] RCA reported a 4% gain in worldwide record sales, to $621.8 million.[76]

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[74] See "Disk Industry Volume Up 15% For '84; Cassettes Are The Key," Variety, Apr. 10, 1985, at 87; I. Horowitz, "'84 A Peak Year for Recordings: Industry Net Shipments Worth $4.5 Billion," Billboard, Mar. 23, 1985, at 1.

[75] "A Year for Records," Fortune, Apr. 1, 1985, at 10.

[76] I. Lichtman, "RCA Records Posts '84 Sales Jump," Billboard, Mar. 23, 1985, at 4.

Warner Communications' Music Group revenues climbed 7%, to $817.57 million, with operating income soaring 32%, in what was described as the "biggest year ever."[77]

The strong upward trend continued in 1985. Led by compact disc sales, retailers and many record companies enjoyed one of their healthiest years ever.[78] In the first half of 1985, gains of as much as 20% over 1984 were reported at the retail level for a cross-section of products.[79] By the end of 1985, the operating income of the records and music publishing group of MCA had reached an all-time annual high, more than doubling over 1984.[80] Warner Record Group 1985 profits were up 26%, with all-time high revenues in the fourth quarter.[81] The phenomenal success of the recording industry last year is underscored by the fact that the number of new titles on albums increased in 1985 for the first time in six years.[82]

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[77] "WCI Music Group Posts Boffo Results for 1984, 4th Qtr.," Variety, Feb. 20, 1985, at 73; S. Sutherland, "Warner Bros. Music: 'Biggest Year Ever,'" Billboard, Mar. 16, 1985, at 6.

[78] K. Terry, "Eye Sharp Contrast in Label Fortunes," Billboard, Jan. 8, 1986, at 1; K. Terry, "U.S. Record Sales Still Upward Bound: Retailers Happy with 1st Quarter," Variety, Apr. 10, 1985, at 87; J. Sippel, "Chains See Ambitious Expansion," Billboard, Sept. 15, 1984, at 3.

[79] J. Sippel, "CD, Video Contribute to Strong First Half," Billboard, July 13, 1985, at 1.

[80] "MCA Inc. Reports Stellar Year," Billboard, Feb. 15, 1986, at 6.

In 1986, the pace continues. CBS Records experienced a "dramatic" 55% increase in profits in the second quarter, which the company described as "solid year-to-year gains."[83] The Warner Record Group posted a new division high in operating income for the first quarter of this year, outstripping last year's high.[84] This year MCA reported its highest first quarter revenues in its history.[85]

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[81] F. Goodman, "Warners: Profits Up 26%," Billboard, Feb. 22, 1986, at 4. WEA International, comprised of the affiliates of Warner Records, enjoyed "a spectacular year worldwide," according to one of the company's executives, with net music revenues increasing by 27%. "WEA International Reports Banner Year," Billboard, Feb. 1, 1986, at 3.

Even though CBS Records, in 1985, did not exceed its extraordinary performance of the year before, it was still enormously profitable, with a strong fourth quarter improvement over 1984. CBS blames the decline on lack of major artists releases and a soft market. "CBS Group's '85 Profits, Revenues Fall: Company Staged Strong Year-End Comeback," Billboard, Feb. 22, 1986, at 4. It should also be emphasized that 1985 performance is being measured against 1984, which was, with the phenomenal success of "Thriller," the Records Group's best year ever.

[82] "RIAA: New LP Titles Up in '85," Billboard, Apr. 5, 1986, at 78.

[83] "CBS Records' Profit Up 55% in 2d Qtr.," Variety, July 16, 1986, at 115.

Thus, even without the presence of multi-million selling albums, record company executives and retailers are reporting that the music industry remains strong on the basis of a broad range of records and that they are selling more records overall.[86] In particular, the new compact disc format has boosted sales in the first part of this year -- with retailers enjoying the bounty of unprecedented consumer demand.[87]

The industry's revitalized health is apparent in the number of platinum (selling one million units) and gold (one half million) albums. In 1985, the RIAA reported, the record industry enjoyed the largest number of platinum albums in five years, and the greatest number of gold albums in four years.[88] An even more significant sign of the industry's creative vigor is that relatively new artists, who had never before made such best-selling albums, earned a full one-third of the platinum and gold certifications awarded in 1985.

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[84] "WCI Music Earnings Rise Again," Billboard, May 10, 1986, at 4.

[85] "MCA Income Jumps," Billboard, May 10, 1986, at 4.

[86] F. Goodman, "Labels Maintain Optimism Despite Void in Mega-Hits," Billboard, Feb. 1, 1986, at 1.

[87] "Sustained Sales Keep CD Sizzling in January Chill," Billboard, Feb. 1, 1986, at 1.

[88] P. Grein, "LP Platinum, Gold Tally is Best in Years," Billboard, Jan. 11, 1986, at 3.

And, again, in 1986, the strength of the industry is undiminished. Over the first half of this year, the number of gold and platinum awards is matching last year's high.[89] In January of this year, for example, the RIAA certified the highest monthly total of platinum albums in three years and, of gold albums, the highest in over a year.[90] Speaking of the "metal awards", the long-time RIAA executive director said, "I've not seen anything as explosive as this."[91] Paced by compact discs, and music video, industry-wide increases over the last four years are marked, with no signs of a return to the slump of the early '80s.[92] Everyone agrees: the

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89 "RIAA Gold, Platinum Awards Running Even With '85 So Far," Variety, July 9, 1986, at 82.

90 P. Grein, "Top Monthly Platinum Tally in Three Years," Billboard, Feb. 15, 1986, at 3.

91 H. Schipper, "First-Timers Mined 34% of RIAA Metal in 1985," Variety, Jan. 8, 1986, at 208.

92 J. Shulman, "Compact Disks Expected To Boost Overall Sales," Variety, Jan. 8, 1986, at 209; "The Record Business Is Solid Gold Again," Business Week, Feb. 25, 1985, at 35; K. Terry, "U.S. Record Sales Still Upward Bound," Variety, Apr. 10, 1985, at 87; K. Terry, "Record Biz Makes A Strong Comeback: Buyers Respond to New Music," Variety, Jan. 16, 1985, at 195.

industry is back.

The current resurgence of the industry's performance demonstrates that the industry's problems over the last few years have had little to do with home taping. Record company executives have pointed to an improved economy, the popularity of the Walkman and the technological shift toward portable music, a decline of interest in videogames,[93] and enthusiasm for new releases, stimulated by wider radio airplay and the emergence of music video.[94] Thus, despite the industry's complaint that home taping was responsible for the slump, many of the industry's problems were external.[95] That the recording industry's performance is closely tied to the health of the economy is no surprise: its own sales data demonstrate that record sales fall in a recession, but that sales soar in a period of economic recovery, such as that of late 1975 to late 1979 and that enjoyed by the country today.[96]

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[93] Record industry executives recognized that videogames inflicted very substantial damage. Estimates of actual dollar losses attributable to videogames range from the RIAA's own figure of $400 million annually to as high as a billion dollars. "$262 Billion Dogfight for Your Leisure Spending," U.S. News and World Report, July 26, 1982, at 47. John Kalodner of Geffen Records said at the time:

> Videogames aren't just part of the problem [with record sales], they're 90 percent of it. It's really scary going to the mall and seeing a deserted record store and the arcade next door is full of kids playing Pac-Man.

"Video Games Gobble Film, Record Profits," Journal of Commerce, Aug. 4, 1982, at 3B.

[94] J. Pareles, "Pop Record Business Shows Signs of Recovery," N.Y. Times, Nov. 28, 1983, at C13.

Two other factors in the resurgence are the industry's recognition -- and movement to correct -- its own failings and its finally beginning to adapt to a new market in which consumers demand portable music. These factors are detailed below. What is clear, however, is that, in shifting the blame for its poor performance to home taping, the recording industry simply misreads its own history and fails to understand the web of economic and social factors that fuel consumer demand for prerecorded music. The industry's current success demonstrates clearly that there is no reason to impose royalties on audio recorders to generate additional revenues that are designed to stimulate creativity. The record companies are now rolling in more money than ever before.

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[95] Retailers, too, are crediting the national economic recovery as being the "paramount" factor in the boom, along with appeal of new releases, diminished competition from videogames, the growth of sales of portable cassette players, and the increased exposure of artists on MTV and other television outlets. K. Terry, "Record Biz Makes A Strong Comeback," Variety, Jan. 16, 1985, at 195.

[96] For example, the number of units sold by the industry rose from 591 million in 1976 to 726 million in 1978. During the 1974-1975 recession years, the number of units sold, and the number purchased per capita, declined. Between 1976 through 1978, an expansionary period, these numbers increased dramatically. The current economic recovery, which began in the first half of 1983, has helped to pull up the recording industry with it.

B. The Recording Industry Is Only Now Making The Changes That The Market Requires

The recording industry has only itself to blame for disappointments with its performance in the early 1980s. At the time, industry leaders recognized that home audio taping was being made a "scapegoat" for the "manifold shortcomings" of the industry.[97] In mid-1982, one retail store manager stated that, "The industry is at a crossroads," and blaming home taping "for its ills is not only patently ridiculous, but also very sad."[98]

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[97] M. McLaren, Variety, July 21, 1982, at 57. Russ Solomon of Tower Records termed home taping and record rentals as "the excuses that record executives and media mavens have offered to describe our long-rumored demise." "Solomon's Wisdom: Music Is Power," Billboard, Apr. 23, 1983, at 4.

[98] C. Carter, "Commentary: Facing Up to Home Taping," Billboard, May 22, 1982, at 14.

That the industry chose to blame home taping for its purported ills is not surprising. Only now is the industry beginning to capitalize on the opportunities created by the boom in portable audio tape equipment. Only now is it selling the stars while cautiously developing new artists. Only now is it finally cutting its costs and starting to operate with greater efficiency. Only now, is it relying on music video, video production, and other innovative promotional tools. And, only now, does it have the exploding market opportunities of the new compact disc technology. It is disingenuous for the industry to clamor for a royalty tax to be paid by home tapers when it was the industry itself -- and not home taping -- that was responsible for the slump in sales of prerecorded music.

1. The Industry Is Finally Exploiting The Market For Portable Music

Today, even though the industry is finally reaping rewards for its belated marketing of prerecorded music in cassette form, consumers are still taping because record companies do not provide them with the readily available, high-quality, portable music that they want. Several years ago, the industry made what was perhaps the most significant and costly marketing error in its history:

it failed to perceive that the introduction in 1980 of the Walkman and other high-fidelity portable cassette players would create a huge demand for high-quality cassettes of the latest releases. Portability became the key word in marketing audio tape equipment in the late 1970s. Sales of portable audio tape equipment almost tripled between 1979 and 1985.[99]

Such dramatic increases in sales of portable players should have alerted the recording industry to the major upheaval occurring in the prerecorded music business. The industry's failure to pick up the signals ended up costing it dearly,[100] and it is still lagging behind the

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[99] Sales have risen annually, from 11.8 million units in 1979 to a projected total of 31 million units by the end of 1985. Electronic Indus. Ass'n, "Consumer Electronics U.S. Sales by Product Category," Table 21, Total Portable Audio Tape Equipment (Jan. 1986). There have been even sharper increases in sales of cassette tape players for automobiles; factory sales have grown from $2 billion in 1981 to a projected $2.8 billion in 1985, with estimates of $3 billion by the end of 1986. Id., Table 24, Total Car Audio Equipment.

[100] One record company marketing director candidly observed,

> [W]e all should have seen it [the cassette revolution] coming two years ago [in 1980] when prerecorded cassette sales started mushrooming . . . .
>
> We failed to see that the public was literally handing us a new market.

C. Tobey, "Commentary: Waging the Cassette Battle," Billboard, Oct. 30, 1982, at 10.

American public in embracing the cassette revolution.

For much of the music that they want, in the portable format that they want, consumers have resorted to home taping.[101] The industry historically has continued to push records and has refused to release the most popular records in cassette form. As recently as the summer of 1985, a very substantial percentage of new releases were not even made available on cassettes.[102] The industry's marketing practices remain static and in stark defiance to changes in consumer preference. Thus, instead of coming to Congress to seek compensation for home taping, the industry might better spend its resources in becoming more attentive -- and adapting -- to consumer demand.

Nevertheless, despite the industry's lethargy, prerecorded cassettes have quickly overtaken albums as the format preferred by music lovers. In 1985, cassette sales rose to an all-time high 339.1 million units, with the dollar value of shipments rising to $2.41 billion, and, in number of units shipped, outpaced LPs by over two to one.[103] Unquestionably, a major factor in the sales resurgence is the mobility of cassette players. As one retailer put it, "[t]he big thing in our business is cassettes. Music is the only thing people can take along with them when they travel."[104]

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[101] The Yankelovich Survey found that 75% cited portability, and 57% cited convenience as "very important" reasons for sometimes using home-recorded tapes instead of records. Yankelovich Survey at 18-19, 69-82.

[102] Even as recently as the July and August 1985 issues of the Schwann catalogue, there were 730 new releases of prerecorded music (not including compact discs) of which 302 were only released in record format.

Further gains could be achieved if the industry improved the quality of its prerecorded cassettes. The sound reproduction of a record is noticeably superior to that of the typical cassette as a result of inferior material and shells, and the inexpensive high-speed manufacturing process the industry uses to produce cassettes.[105] To make matters worse, cassettes have cost more than records, so consumers have been offered a product of inferior quality that carries a premium price.[106] Not satisfied with low quality and high price, consumers make their own recordings by selecting high-quality recorders and tape and by duplicating at real time.[107] Again, the public tapes because the industry refuses to satisfy marketplace demand.

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[103] I. Horowitz, "RIAA: '85 Shipments Flat," Billboard, Mar. 29, 1986, at 1. See also "Disk Industry Volume Up 15% For '84; Cassettes Are The Key," Variety, Apr. 10, 1985, at 87; "RIAA Figures: Cassettes Paced A Record '84," Billboard, Apr. 13, 1985, at 1.

[104] K. Terry, "Disk Biz Basking In Sales Glow: Retailers Report Gains of 15-20%, Units Up Too," Variety, Aug. 29, 1984, at 1.

[105] The use of inferior quality materials causes inexact tracking during play; the speed at which prerecorded cassettes are duplicated -- 64 times normal speed -- causes inferior quality on playback. See Video and Audio Home Taping, supra note 41, at 443 (statement of Edward J. Foster, President, Diversified Science Laboratories).

2. The Industry Is Selling The Stars And Is Moving Cautiously On Signing New Artists

The industry has had fabulous results with the superstars of the 1980s -- even as it is complaining of home taping. Though home taping has continued, the mega-million album sales of the last few years demonstrate conclusively that the industry is wrong when it blames home taping for its ills.

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[106] See I. Lichtman, "Consumer Cassette Cost Often Greater than LP," Billboard, May 1, 1982, at 9.

[107] Jan Timmer, President of PolyGram International, recognizes that the poor quality of prerecorded music is a significant factor in home taping. He believes that compact discs will not only undermine home taping because CDs are so convenient, but also that the superior sound reproduction on CDs creates a tremendous opportunity for record companies: "If we can convince a major portion of the public that disc is better than tape, then we create longevity for our industry." Gramophone, Nov. 1985, at 601.

Michael Jackson's "Thriller" is the most popular album of all time, with sales in excess of twenty million.[108] Other albums, by Bruce Springsteen, Prince, Lionel Richie, Madonna, Tina Turner, Huey Lewis and the News, and Phil Collins have led a fabulous couple of years for the industry.[109] As noted above, platinum and gold album certifications rose sharply in 1984; in 1985, they were the best in many years, with the first half of 1986 keeping up the pace.[110]

Industry executives point to industry caution in signing new artists as a major factor in industry success. Attentive to the skyrocketing costs of promoting new artists, the larger record companies have concentrated attention and resources on acts that are deemed to have a good chance of making it big. RCA vice president Paul Atkinson explained the new strategy: "[w]e can't focus on 50-60 artists . . . so instead we focus on a few, and it pays off."[111] Accordingly, prudent management and economic realities are the leading factors in the industry's decision to release fewer records.[112]

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[108] K. Terry, "Record Biz Makes A Strong Comeback," Variety, Jan. 16, 1985, at 1. Seven of the nine songs on "Thriller" were released as singles, and each song received significant airplay and achieved "gold" status.

[109] The ten million copies of Prince's "Purple Rain" that were sold in 1984 established a single year's high for domestic sales of an album. "Inside Track," Billboard, Feb. 23, 1985, at 74.

[110] *See* "RIAA Gold, Platinum Awards Running Even With '85 So Far," Variety, July 9, 1986, at 82; P. Grein, "LP Platinum, Gold Tally is Best in Years," Billboard, Jan. 11, 1986, at 3; P. Grein, "Big Jumps in Platinum, Gold, RIAA '84 Totals," Billboard, Jan. 12, 1985, at 1.

At the same time, the industry has begun to realize its mistakes of the early 1980s, when it was more concerned with "playing it safe" than with keeping the public interested in new music.[113] Thus, record companies are now attempting to strike the appropriate balance between the need to bring new music and artists to the market and the new cost control imperative.[114] While curtailing advances for new acts, the industry is experimenting with development deals and other new financing options. The end result: a wiser, leaner industry is enjoying unprecedented success.

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[111] H. Schipper, "First-Timers Mined 34% of RIAA Metal in 1985," Variety, Jan. 8, 1986, at 208.

[112] J. Zaslow, "New Rock Economics Make It Harder to Sing Your Way to Wealth," Wall Street Journal, May 21, 1985, at 1; "The Record Business Is Solid Gold Again," Business Week, Feb. 25, 1985, at 35.

[113] See E. Kleinman, "Commentary: Playing It Safe -- And Dull," Billboard, June 26, 1982, at 18. See also R. Holmes, "Commentary: On Rekindling Old Passions," Billboard, June 12, 1982, at 16.

[114] P. DiMauro, "Disk Labels Play Cautious Game," Variety, Feb. 13, 1985, at 1.

3. The Industry Is Cutting Costs And Is Beginning To Operate More Efficiently

The new caution in signing artists and in spending for promotion is reflected throughout the industry. In 1977-78, performers were signed in extravagant deals and record companies generally hoped for success; millions of records were pressed in 1978, and then returned unsold.[115] As a result, artist rosters were trimmed and record companies reduced their staffs. CBS closed two factories and half its branch sales offices.[116] Inventories were tightened.

At the same time, the industry adopted new practices with respect to their relationship with retailers. The record companies demanded faster payment from retailers, sometimes as soon as sixty days after shipment. This contraction in credit was accompanied by a new "returns" policy that greatly limited -- to only 20% -- the number of unsold records that could be returned for credit from the manufacturer.[117] These policies have increased cash flow to the record companies and contributed to the recent profitability of the industry. They have also had, however, a somewhat depressive effect on retailers' ability to market aggressively. Retailers have been more inclined to be conservative in their stocking and ordering decisions and are more reluctant to order releases by new or unknown artists; they simply cannot take the risk that stock will sit on their shelves.

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[115] J. Pareles, "Pop Record Business Shows Signs of Recovery," N.Y. Times, Nov. 28, 1983, at C13.

[116] *See* S. Salmans, "The King of CBS Records," N.Y. Times, Jan. 22, 1984, at F7 (CBS Record President Yetnikoff boasting that CBS "did cost-cutting that would make Chrysler proud").

These new record company policies have made it more difficult for retailers to supply the records that the public wanted. Instead, consumers taped to obtain music by new artists. The industry should not be heard to complain about practices that were caused by the very efficiency measures that have resulted in its unparalleled success.

4. Music Video And Innovative Promotional Practices Have Fueled Industry Success

Video promotion, perhaps more than any other factor, has been an engine of industry success. The most powerful tool for marketing records is music video, with its strong appeal to the demographic group -- 15- to 24-year-olds -- that buys the most records.[118] Through music video seen on television -- like the Warner Amex cable channel Music Television (MTV) or NBC's "Friday Night Video" -- recording artists have benefitted from substantial exposure that has driven demand upward. A broader range of artists is being publicized.

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[117] "Record Industry Nervous As Sales Drop Fifty Percent," Rolling Stone, Sept. 30, 1982, at 69, 79; "Record Business Slumps as Taping and Video Games Take Away Sales," Wall Street Journal, Feb. 18, 1982, at § 2, at 31.

Cutting back on traditional tours, record companies are, therefore, spending significant amounts on the production of video clips for promotional purposes. An emerging promotional phenomenon is the "video tour" -- packages of video clips sent around the country to rock video clubs in lieu of live performances.[119] As the costs of traditional concert tours skyrocket, the industry is finally beginning to understand and use some of the technologies that are changing -- and benefitting -- the entertainment industry.

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[118] J. Zaslow, "New Rock Economics Make It Harder to Sing Your Way to Wealth," Wall Street Journal, May 21, 1985, at 1. Music video is especially important for promoting new artists because, according to Warner Brothers publicity director Bob Merlis, it gives the public "more to latch onto." H. Schipper, "First-Timers Mined 34% of RIAA Metal in 1985," Variety, Jan. 8, 1986, at 208.

[119] K. Terry, "Record Biz Makes A Strong Comeback," Variety, Jan. 16, 1985, at 195.

The advent of video programming on MTV has also reinvigorated the most traditional of promotional tools -- radio airplay. Feeling the competition from music video, radio programmers have become more adventuresome, playing music that the public has heard -- and seen -- on television. As a result, said one independent record producer, "[p]eople got turned on to all kinds of music that they never heard before."[120]

The video boom has also helped the industry in other ways. The rock video dance sequences in the film "Flashdance," for example, were used as both a commercial for the movie and to promote the 4.5 million selling soundtrack.[121] Music videos are used as trailers in theaters before being aired on cable or over-the-air television outlets. There is also a synergistic relationship between prerecorded cassettes of music video titles and the records and tapes containing the music on those titles, with the video and audio works cross-promoting each other.[122] Moreover, record retailers are now carrying prerecorded videocassettes, a development that not only has brought many new customers into stores but also has increased the opportunities for industry cross-promotion between video works and prerecorded music.[123]

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[120] J. Pareles, "Pop Record Business Shows Signs of Recovery," N.Y. Times, Nov. 28, 1983, at C13.

[121] *Id.*

The industry, therefore, has ever-so-slowly begun to recognize that the new recording technologies are its golden goose. Whether in video, audio, or in technologies that marry the two, the industry is gradually understanding that it should use and adjust to technological developments, not turn back the clock to the days when its sole product was on vinyl and "creative promotion" was sending an album to a "Top-40" radio station. By working with -- and not fighting -- the new technologies, the industry can surpass even the tremendous successes of the last few years.[124]

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[122] Vestron Video's prerecorded videocassette, "Making Michael Jackson's 'Thriller'," which has been marketed through video retail outlets, is among the biggest selling videocassettes of all time, and helped to fuel, while it capitalized on, demand for the "Thriller" album.

[123] J. Bressi, "New Entertainment Lines Promise Greater Prosperity For Retailers; Music Video Starting To Happen," _Variety_, Jan. 16, 1985, at 195.

[124] In the middle of the recording industry slump of the early 1980s, the president of a music industry public relations firm criticized as "grotesque" the industry's failure to adapt to the technological

5. The Compact Disc Is Leading The Industry On To Even Greater Heights

The compact disc ("CD") phenomenon may be the best example of how the recording industry benefits from new technologies. The demand for CDs is exploding, and it is now the fastest-growing configuration in the industry.[125] CD sales reached $320 million last year,

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[footnote continued]

changes of the new market:

> We are in the midst of several technological revolutions which will expand the market for prerecorded music dramatically -- in fact, which have already expanded it. . . . We are . . . fixated on the notion that the record is the primary vehicle for prerecorded music and are regarding all other formats as a menace which, if we wish hard enough, protest loudly enough or establish enough committees, will go away. But the new formats are opening up vast new opportunities for the sale of prerecorded music. . . . [however] we're selling less prerecorded music.
>
> Why? The answer is simple. We are not servicing the new market.

H. Bloom, "Commentary: Selling Music, Not Records," Billboard, Mar. 13, 1982, at 16.

[125] In 1985, 18 million compact discs were shipped, contrasting with 5.8 million in 1984 and fewer than one million in 1983; there are now 5000 titles on CD, compared with only 1000 at the end of 1984. G. Fabrikant, "CD Industry's Growing Pains," N.Y. Times, Feb. 11, 1986, at D1; J. Shulman, "Compact Disks Expected To Boost Overall Sales," Variety, Jan. 8, 1986, at 209. A Newsweek survey estimates that the incidence of compact disc players among stereo owners will double in 1986. I. Horowitz, "Survey Predicts CD Player Boom," Billboard, Sept. 7, 1985, at 3.

tripling the $103 million in 1984 and a monumental leap from the mere $17 million of 1983.[126] By the end of this year, some experts predict, CD volume may surpass that of albums, with nearly a 25% market share.[127] In just four years, the CD format could account for up to 60% of the industry's sales.[128]

CDs are also contributing more and more to the bottom line, with many retailers reporting consistently that they are responsible for double-digit percentages of their gross.[129] During the 1985 Christmas selling season, record retailers reported "phenomenal" sales in the CD format, estimating that up to 35% of overall volume was CD.[130] And, in early 1986, there were reports that CD sales are surpassing those of cassettes.[131]

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[126] G. Fabrikant, "CD Industry's Growing Pains," N.Y. Times, Feb. 11, 1986, at D1; J. Shulman, "Compact Disks Expected To Boost Overall Sales," Variety, Jan. 8, 1986, at 209; K. Terry, "Eye Sharp Contrast in Label Fortunes," Billboard, Jan. 8, 1986, at 1.

[127] K. Terry, "Exec Predicts CD Soon Will Surpass LP," Variety, June 25, 1986, at 75.

[128] G. Fabrikant, "CD Industry's Growing Pains," N.Y. Times, Feb. 11, 1986, at D1.

[129] For retailers who aggressively promote CDs, they account for 25% of their sales. I. Horowitz, "Survey Predicts CD Player Boom," Billboard, Sept. 7, 1985, at 3; J. Sippel, "CD, Video Contribute To Strong First Half," Billboard, July 13, 1985, at 1.

[130] G. Mayfield, "Yule: Records Mild, Video Wild," Billboard, Jan. 11, 1986, at 1.

The profits from the CD explosion are also being felt back in recording industry executive suites. One Warner executive boasted that CDs cost about $2.50 and are shipped for $8, a marked improvement over the comparable numbers for tapes and records, which have a raw cost of $1 and a shipping price of $5.[132] By the reckoning of some record industry executives, the industry enjoyed up to $80 million in profits last year (out of $300 million plus sales) from CDs alone.[133]

The compact disc phenomenon has been particularly important for classical music. In 1985, for example, PolyGram Classics (which accounts for up to half of the classical music business in the U.S.) enjoyed a 35% increase over 1984 -- with CD providing 48% of the total dollar volume; the expected breakdown for 1986 is that 65% of that company's classical music sales will be in the new format.[134] As classical and other music is reissued on CDs, buyers are brought into record stores, where they are exposed to new music or rediscover their favorites.

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[131] "Sustained Sales Keep CD Sizzling in January Chill," Billboard, Feb. 1, 1986, at 1.

[132] "The Record Business Is Solid Gold Again," Business Week, Feb. 25, 1985, at 35.

[133] As reported in The New York Times, the recording companies had a $3 to $4 profit on the 20 million CDs they sold last year. G. Fabrikant, "CD Industry's Growing Pains," N.Y. Times, Feb. 11, 1986, at D1.

For the industry, the CD phenomenon means that companies have additional, highly-lucrative opportunities to sell music to consumers in yet another format. CBS Records research studies show that almost 80% of the owners of CD players are purchasing CDs containing selections already in their collections.[135] Retailers love the CD format because new owners of CD players "come in by the droves" to replace their collection.[136]

Yet, the record companies have been exceedingly slow to meet the demand for CDs, a tardiness that has hamstrung significantly sales increases.[137] Retailers are complaining, the consuming public wonders why more product is not available on CD, and improvement in the situation, if any, is long-term.[138] In short, the record companies could be doing even better -- if only they were swifter, and more adaptable, in moving to give the public what it wants.

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[134] I. Horowitz, "The World of Classical Music," Billboard, Nov. 16, 1985, at C-1. In every segment of the classical music industry, the contribution of CD to reinvigorating sales, to encouraging mature individuals to return to record stores, is lauded as phenomenal. I. Horowitz, "Classical Status: Label Reports," Billboard, Nov. 16, 1985, at C-3.

[135] J. Shulman, "Compact Disks Expected To Boost Overall Sales," Variety, Jan. 8, 1986, at 209.

[136] E. Paige, "Retailers' Classic Love Affair," Billboard, Nov. 16, 1985, C-4.

In sum, the story remains the same -- with CDs, with portable players, with video/audio equipment, and with home taping. One after another, the recording industry is handed opportunity after opportunity to sell to the public. The industry, however, fails to learn the simple truths: technology is not a threat, but a friend and home taping is not the cause of industry failings, but a reason for industry successes. The most important lesson, however, is that consumers should be lauded for boosting the industry (with all of its inadequacies) to record highs, not thanked for their contribution to industry health by being forced to pay millions of dollars in additional tribute.

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[137] G. Fabrikant, "CD Industry's Growing Pains," N.Y. Times, Feb. 11, 1986, at D1. Warner Records speculated, for example, that it could have sold twice as many CDs of a recent hit album by the group Dire Straits, but that it simply could not get them made; lost sales and profits were the not-so-surprising result. Id.

[138] H. Schipper, "CD Shortages Continue, Limiting Growth of Sales," Variety, Jan. 22, 1986, at 73.

V. Only Wealthy Recording Companies, Artists, And Composers Would Benefit From A Royalty Tax -- Not The Artists Or Music That May Need Additional Support

The recording industry has tried to argue that a royalty tax is needed to aid composers and artists or to give it the resources to produce new or non-mass market music. The fact of the matter is that whatever small benefit struggling artists and composers would receive from such a tax would be insignificant in comparison to the millions of dollars that would flow to the real beneficiaries of the tax: the big six record companies, a few singer/songwriters, and already well-to-do publishing companies. Given the traditional tension between the interests of the copyright owner-record companies, on the one hand, and those of the composers and lyricists, on the other, Congress should be wary of any representations that S. 1739, even as amended, would actually bestow some benefit on the creative talent.

The current version of S. 1739 would distribute the lion's share of royalty taxes to the music publishing companies and record companies that own the overwhelming majority of copyrights in musical works -- compositions by songwriters -- and sound recordings -- prerecorded music. With respect to the relationship between composers and publishers, the percentage allocations of the bill would only reinforce current contractual arrangements. S. 1739 would do nothing to improve the bargaining position of struggling artists, and may erode what little power they do have.

The set allocation of the Musical Work Fund, one of the three funds that S. 1739 would establish, would, for example, reinforce the extraordinarily strong market position of music publishing companies. Such companies act as middlemen for marketing the works of composers to performers -- singers and instrumental groups. In return, composers typically sign away to these publishers 50% of all revenues from their copyrighted works. S. 1739 supercedes all privately negotiated contractual arrangements and actually would require this 50-50 distribution. Thus, the bill would further enrich these publishers -- who do extremely well in a business in which they receive revenues generated by the efforts of composers in their stable -- rather than adequately reward or encourage the composers themselves.[139]

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[139] Indeed, business is so good for publishing houses that

Even with a scheme that mandates that 50% of the Musical Work Fund be paid to songwriters, struggling composers and lyricists would see very little of the proceeds. It is likely that only a handful of songwriters would profit from a royalty tax: notwithstanding the 20% payment to Incentive Class claimants, the vast bulk of the home taping royalties would be paid to these already successful artists, who are certainly the least likely to be spurred on to new creative heights by payments from the royalty fund.[140] How much more incentive to create music does Michael Jackson require, above and beyond the $70 million he received from "Thriller?"

[footnote continued]

the owner of music publisher Chappell and Co. confessed that "[Y]ou can't lose money" and "[I]t's the most unbelievable business." S. Salmans, "A Song Plugger's Biggest Play: His Return as Boss," N.Y. Times, June 4, 1985, at D1.

[140] In 1979, for example, Warner Records paid 49% of the so-called "mechanical royalties" (paid by record companies to composers each time a song is recorded on an album or tape) to just 16 singer/songwriters and 81% went to publishers controlled by singer/ songwriters. Prehearing Memorandum of the Recording Indus. Ass'n of America, CRT Docket No. 80-2, 29-30 (filed May 5, 1980) [hereinafter "RIAA Memorandum"]. To avoid paying 50% of their royalties to an established publishing company, singer/songwriters may establish their own publishing companies. This option is generally available only to those singer/ songwriters with substantial marketplace clout.

The primary beneficiaries of the royalty tax would be the large record companies, which own most of the copyrights in sound recordings: CBS, RCA, Warner, Polygram, Capitol, and MCA.[141] Together these six companies, through distribution agreements, control 82% of the market.[142] They would get an equally large share of the 60% of the Sound Recording Fund (which is, in turn, 75% of the whole pool) that is to be paid to record companies.

Even with the new distribution formula, the structure of the recording industry diminishes the likelihood that struggling performers or artists will be substantially better off. Although 40% of the Sound Recording Fund is earmarked for featured artists, whether artists realize a net gain ultimately will depend on negotiations between these mega-companies and the performers.

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[141] CBS distributes the Columbia, Epic, and the independent Chrysalis labels; RCA distributes the RCA-Victor, Arista, and the independent A&M labels; Warner distributes the Warner, Atlantic, and Elektra/Asylum labels; Polygram distributes the Mercury, Casablanca, Polydor, Capricorn, RSO, and several classical labels; Capitol distributes the EMI, Capitol, and Ariola labels; and MCA distributes the MCA, Coral, and the independent Motown labels.

[142] L. Landro, "Merger of Warner Unit, Polygram Angers Troubled Record Industry," Wall Street Journal, Apr. 12, 1984, at 33.

The bargaining power that large record companies wield over new artists will undercut the effort to distribute royalties to performers under S. 1739. Although the bill purports to supercede contractual arrangements between artists and the record companies, the companies can still use their clout to use the distribution of proceeds from the royalty taxes as an offset against any other payments that the companies will be willing to make to new artists.

That the industry will not hesitate to use payments under S. 1739 as an excuse for exacting contractual concessions from artists is demonstrated by a front-page article in The Wall Street Journal: even a big new star -- Patty Smyth -- after three years in the business, two albums, and several major tours, has earned less than $150,000 out of a total retail gross of exceeding $10 million.[143] The notion of Incentive Class payments to the most "struggling" of artists does nothing to change the relative bargaining positions of performers and the record companies. Overall, therefore, despite the fact that consumers will pay hundreds of millions of dollars in new taxes into a royalty pool, it is unlikely that struggling artists will see any improvement at all in their economic lot.

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[143] J. Zaslow, "New Rock Economics Make It Harder to Sing Your Way to Wealth," Wall Street Journal, May 21, 1985, at 1.

Moreover, and as to the monies that the record companies will receive from the Sound Recording Fund, there is nothing to prevent the industry from using the proceeds for anything other than to boost dividends to shareholders or to line the pockets of highly-paid executives. If the industry were genuinely interested in developing and recording classical music, or other music that is aimed selectively at narrower market segments, it could do so at present, with the record revenues and profits it is now enjoying. Neither the pending legislation nor the industry would earmark the money that is collected. It is entirely predictable, therefore, that those additional funds will not stimulate the production and promotion of innovative or specialized music, but, rather, will fall into corporate treasuries.

Given the flow of industry revenues, then, it is improbable that any home taping royalty will confer substantial benefits on struggling artists or encourage creativity. The recording companies themselves have been quite adamant that increases in compensation for composers under the Copyright Act should not be based on "the sympathetic imagery of the struggling songwriter."[144] The RIAA opposed any increase in the mechanical royalty rate because:

> An increase in the mechanical rate will inevitably result in enormous benefits for singers/songwriters who are already richly rewarded for their creative efforts . . . . The struggling composer, on the other hand, will see little measurable benefit from an increase, and might actually suffer harm.[145]

If it pays attention to its own words, then, it is difficult for the recording industry to be at all persuasive in justifying a royalty tax on the ground that it will aid struggling artists and composers or develop specialized music. Although any such argument is intended to arouse congressional sympathies, it is belied by the facts. Despite the efforts of those who have amended S. 1739 to embrace a royalty distribution formula, the harsh reality is that the industry is highly concentrated, that the industry has never been that sympathetic to the creative artists, and that, in any event, the vast bulk of the proceeds will be paid to the most successful performers, lyricists, and composers -- those who need the money the least. A realistic, candid appraisal of the royalty distribution scheme of the amended S. 1739 -- and not an emotional appeal -- reveals that those individuals and musical works that could genuinely benefit from additional industry support would receive little money from a royalty pot.

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[144] RIAA Memorandum, at 1.

[145] _Id_. at 25-26.

VI. The Proposed Royalty Tax Is Arbitrary, Unfair, And Unworkable

Like its predecessors, the amended version of the Home Audio Recording Act (S. 1739) would impose a substantial royalty tax on audio recorders that would be distributed to the owners of copyrights in musical works and sound recordings, to performers, and to the guilds. The amount of the tax -- 5% of the first domestic sale price of recording equipment and 25% of that for dual cassette recorders -- is entirely arbitrary, not even pretending to relate to any claim for compensation allegedly owed as a result of home taping. Moreover, the burden of the tax would fall equally on individuals who use audio equipment in conjunction with the home taping of prerecorded music and those who use those products for other purposes.

A. Overview Of Problems With Proposed Remedy

The royalty tax proposal of the amended S. 1739 is burdened with a number of irremediable problems, which are set out in brief in this subsection, and are explored at some length below. Many of these problems repeat defects of past proposals or derive from trying to remedy them. They include: 1) an arbitrary and unfair approach to setting the level of the tax; 2) the overbreadth of the tax and its application to those who do not use or tape copyrighted material; and 3) defects in the mechanism for distributing the funds collected. By attempting to remedy past flaws, the purported solution creates new and even worse problems.

1. The Amount Of The Proposed Royalty Is "Pulled Out Of Thin Air" And Bears No Relation To Any Alleged Harm From Home Taping

Proposals of previous legislative sessions would have established a complex administrative procedure for calculating the amount of any royalty tax. There were, however, a host of legal, administrative, and anticompetitive problems with the negotiation and arbitration process that would have set the level of the tax. S. 1739 attempts to avoid these problems by simply codifying the amount of the tax, essentially "pulling it out of thin air." As discussed earlier,[146] there has never been any independent assessment of the economic consequences of home taping -- the amount of various types of taping, the impact of taping on sales of prerecorded music, and, most importantly, the stimulative effects of taping.

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[146] See supra Section III.A.

2. The Purported "Solutions" Of S. 1739 To The Overbreadth Of A Royalty Tax Are Unworkable

Although S. 1739 contains various "exemption" provisions in an attempt to remedy the overbreadth problems of previous bills, it is completely unsuccessful in this regard. Preliminarily, the effort to limit the applicability of the royalty tax is itself a major concession by the recording industry that audio recorders have significant uses besides the taping of copyrighted music. Having acknowledged that past proposals had a major flaw that had to be addressed, the recording industry has not now succeeded in formulating any workable solution.

Rather, S. 1739 proposes what appear to be deceptively "simple solutions" to the overbreadth problem: 1) imposing a tax only on audio equipment that is "suitable" for taping copyrighted material and 2) exempting particular users from the tax. Like many so-called "simple solutions," however, those contained in S. 1739 solve nothing at all and create their own problems. Several major defects are apparent:

o Classifying recording devices "suitable" for home recording will distort technology and will inevitably involve the Copyright Royalty Tribunal ("CRT") in the oversight of product standards and development in the electronics industry -- a role both unduly intrusive and potentially stultifying to innovation and competition.

o Definitions of "exempt users" are imprecise and likely to result in abuse and a need for government monitoring.

o Administering the exemption scheme will be both complex and costly at all stages in the distribution chain, from the manufacturers down to the small retailers. Ultimately, the burden of such costs will fall on consumers. Will, for example, rebates to "exempt" users be issued directly to consumers or to retailers? How can the scheme be administered when the responsibility for paying the tax in the first place lies with the manufacturers and yet, as a practical matter, the responsibility for granting exemptions is in the hands of retailers?

o The potential for abusing and evading such "special product taxes" is great. These problems should be studied carefully by Congress before another unworkable tax is imposed on the public.

3. The CRT Distribution Scheme Is Hopelessly Flawed And Infeasible

Previous legislative proposals for disbursing the funds collected also had many and substantial defects. Although there has been an attempt to mitigate some of these problems in the amended version of S. 1739, the principal flaws are simply repeated.

o Having the CRT disburse the funds entrusts that responsibility to an agency that has been so plagued with lack of staff, expertise, and continuity that legislators, as well as one of its former chairmen, have called for its abolition.

o The distribution scheme will be time-consuming and subject to disputes because, even though S. 1739 calls for measuring the demand for and level of home taping of copyrighted material, there is no way of accurately doing so.

o The existence of the CRT itself raises significant problems, including the violation of the constitutionally-mandated separation of powers among the three branches of government. (S. 1739 would allocate certain "judicial" authority -- which is properly reserved only for federal courts created under Article III -- to the CRT, which is a "legislative" entity created pursuant to an exercise by Congress of its Article I power.) If these issues are not fully explored prior to enactment, Congress is likely to find itself enmired in the task of repairing legal and institutional defects, as it was so painfully required to do with the bankruptcy courts.

4. S. 1739 Unfairly Makes The Electronics Industry Liable For Home Taping

One major conceptual problem with previous proposals is, as well, left unaddressed by the amended version of S. 1739. The bill deceptively labels itself as granting consumers an "exemption" -- at the same time that it would tax them. As a practical matter, the public is made "liable" for home taping practices in which, over the last few years, it has engaged freely and with legislative imprimatur.

Behind this ruse of a "consumer exemption," however, S. 1739 expands the concept of contributory infringement to impose a tax on hardware manufacturers, who, the bill apparently contemplates, should be made liable for the activities of ultimate consumers. This notion is inconsistent with the Supreme Court's approach to contributory infringement, as enunciated in Sony.

B. The Amount Raised By The Tax Bears No Relation To The Harm Allegedly Caused By Home Taping

The purpose of S. 1739 is to compensate copyright owners for losses alleged to result from home taping. The amount of any such losses, as discussed in detail above, see supra Section III.A., have never been ascertained, either in the aggregate or for individual copyrighted musical works and sound recordings. One reason why it is impossible to devise a truly "compensatory" scheme is because these figures cannot be determined.

The assumption of "harm" that underpins S. 1739, however, makes no effort whatsoever to assess objectively the amount of damages, if any, suffered by copyright owners from home taping. Instead, it simply picks an arbitrary, and large, number as the amount of the levy and then proceeds to impose that tax on manufacturers, importers, and, ultimately, consumers of recording equipment.[147]

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[147] The recording industry stands to realize a windfall of hundreds of millions of dollars annually should S. 1739 be enacted, on top of its multi-billion dollar revenues. The industry claims that the levy will make up only half of its losses from home taping, but, as described above, its estimates of those losses are highly inflated. See supra Section III.A.5.

Consumers will surely object to any tax on home taping -- a practice legitimated by Congress in 1971 and implicitly condoned by the recording industry. They are, however, likely to become even more aggrieved by a bill that simply pulls what purports to be a "compensatory" tax" out of "thin air." Policymakers should not take the industry's word for the amount of any alleged harm. If there is to be no administrative determination of the economic consequences of home taping -- including its stimulative effects -- then Congress at least has the responsibility for addressing that issue.

The arbitrariness of codifying the amount of the levy is not, however, remedied by the provision that the CRT is empowered to adjust the statutory amounts five years after enactment, and every five years thereafter. First, the royalty scheme will have a distortive impact on technology.[148] Thus, given the phenomenally rapid pace of technological developments, the harmful effects of the levy will be felt by consumers and manufacturers in the course of the initial five-year period. Hence, even in the highly unlikely event of the CRT's eventually deciding to adjust the levy downward, the damage to the interests of the public would have long since been done.

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[148] *See infra* Section VI.C.1.

Although the statutory criteria that the CRT is to take into account in adjusting the royalty fee include "reasonable estimates" of the amount of devices not used for home taping, inclusion of that factor in no way solves the problems of unfairness and overbreadth inherent in the proposal. First, there is nothing by which to judge the "reasonableness" of any estimate. Moreover, based on what is now known about the CRT and the way it operates, it is unlikely that it would have the information, or resources and expertise, that would be necessary for it to make any such estimates.

C. It Is Inequitable To Impose A Royalty Tax On All Audio Recorders And The Proposed Exemptions Would Be Unfair And Unworkable

A royalty scheme imposed on all audio recording devices would be unfair because it would not and could not differentiate between recorders used for the home taping of copyrighted material and that used for other purposes. As highlighted above,[149] home taping of copyrighted music is a minority use of audio recorders. Nevertheless, the proposal contemplates that consumers would have to pay the royalty tax every time they purchased a tape recorder, whether to record a flute lesson, telephone messages, letters, lectures, dictation, or to store or run computer programs.

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[149] See supra Section III.A.2.

The inequity of a royalty system is most evident in the case of the significant number of home tapers -- 23% -- who never tape prerecorded music.[150] There is no justification for subjecting these home tapers to a tax intended to obtain compensation for an activity in which they never engage.

1. The Proposed Exemption For Equipment That Is "Unsuitable" For Home Taping Would Affect Few, If Any, Products, Is Without A Meaningful Technical Basis, And Would Distort Technology

The exemption in S. 1739 for equipment that is "unsuitable" for home taping is so narrowly drawn that it is quite possible that no recorders would ever qualify for it.[151] Virtually every recorder can be used for home taping. Hence, any classification system would be inherently arbitrary.[152]

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[150] This inequity would be most pronounced for older tapers, who use a substantially higher proportion of their tapes for recording something other than prerecorded music.

[151] The CRT is authorized to exempt those "audio recording devices, if any," that, "on the basis of technical criteria that are relevant to the purposes of this section, are found to be unsuitable for making audio recordings by individuals for private use."

[152] Perhaps a tiny number of the lowest quality microcassette recorders would satisfy the CRT's concept of "unsuitability"; in fact, however, there are no objective technical grounds for classifying equipment into two discrete classes, those "suitable"

This exemption appears to be a concession to the many uses people have for recorders that have nothing to do with recording copyrighted music. Actually it is no concession at all, for it will leave fully taxable the great bulk of machines, which _may_ be used for taping prerecorded music -- even if they never are.

Taping technology is readily adaptable to novel applications and it delivers remarkably high fidelity at a low price. These are the very characteristics that are responsible for the recording industry's most important new markets of the last two decades. Exempting from the proposed tax only those devices that record sound poorly, therefore, is scant exemption indeed.

Moreover, imposing taxes on recorders that are "suitable" for home taping would create substantial incentives for manufacturers to alter or reconfigure their products to avoid the levy. Thus, taxing some products on the basis of technical characteristics will distort technological development in consumer electronics. Furthermore, the classification scheme of S. 1739 would require the CRT to conduct frequent and detailed investigations so that it could draw lines

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[footnote continued]

and "unsuitable" for home music taping.

between a shifting marketplace population of "suitable" and "unsuitable" products.

There is a significant danger that any classification that relies on technology at a single point in time will be overtaken by subsequent developments or will skew future development away from improvement of devices or tape that might become burdened by royalty taxes. The proposal would almost inevitably distort the development of the consumer electronics industry beyond natural marketplace demand: manufacturers of both compact systems and separate tape decks would have an incentive to put the "core" of the tape recording apparatus into discrete minimum-cost units to avoid the tax on the consumer's entire system.

Even without the exemptions for "unsuitable" recording devices, S. 1739 would present the CRT with difficult problems in line-drawing. For example, it would seem unfair to impose the tax on the basis of the entire cost of an integrated "compact system" that, in one unit, includes a cassette deck, amplifier, tuner, turntable, and speakers. If whole systems were taxed, however, their manufacturers would be at a competitive disadvantage compared to manufacturers of separate components, of which, presumably, only the tape deck would be taxed.

2. The Proposed Classification Scheme Would Require The CRT To Gather Commercially Sensitive Information About Products And Product Developments

The exemption for recorders that are unsuitable for taping copyrighted material will require the CRT to become expert in recording technologies and developments. Manufacturers will be required to submit to the CRT proprietary information about the characteristics of new recording equipment products. It may be difficult to provide adequate safeguards against disclosure of such commercially sensitive information; indeed, it may be incompatible to maintain the confidentiality of product information and to assure fairness to various affected interests. There would, for example, be no way for one manufacturer to be assured that other companies are fairly classifying their own products. Thus, one result of the proposed exemption scheme may be to force proprietary product information into the public domain, with the serious consequence of impairing the competitive relationships that now characterize the audio equipment market.

To evaluate the difficult issues of appraising the "suitability" of particular products for recording copyrighted materials, the CRT would probably need to obtain assistance from other entities in the government that would have the requisite technological expertise. It is, however, unlikely that any governmental organization presently has the staff or expertise necessary to evaluate what are rapidly-evolving developments in the field of consumer electronics.

Governmental oversight of the process of developing products, which S. 1739 would require, would be intrusive and likely to stultify competition and new entrepreneurial activity. Creating such a new bureaucratic process is completely contrary to the premise that the heavy hand of regulation should be lifted from business.

3. The Proposed Exemption For Decoder Chip Devices Would Completely Disrupt The Equipment And Prerecorded Music Markets

S. 1739 also proposes a quick technological "fix" as an alternative to the royalty; by including a decoder chip in a recorder, a manufacturer would be exempted from paying a royalty tax on that device. This proposal is ill-thought out and would wreak havoc on the retail industry.

The technology depends on implanting a signal in prerecorded music to disable a decoder chip recorder from recording the music. The proposal, then, apparently contemplates two sets of hardware -- some with, some without the chip -- and two sets of software -- some with, some without the signal. Records, tapes, and compact discs without the signal -- which could be taped on machines with (or without) the decoder chip -- would be more expensive than their encoded counterparts. Two-tier marketing and pricing for software is the predictable result, therefore, of the decoder chip proposal. Customer confusion and added burdens for retailers of hardware and software is the equally inevitable consequence.

The consumer will be forced to make a series of difficult choices. First, he must choose among the hundreds of models of tape recorders on the market. Once a particular model is selected, the consumer might well be forced to decide between paying the recording tax up front by buying a machine without the chip or, if he buys a decoder chip recorder, by subsequently paying a premium for each purchase of an unencoded recording that he might wish to tape. Thus, in weighing the economic soundness of buying a "tax exempt" decoder chip recorder, the customer must determine his home taping habits ahead of time, a task that is impossible.

Second, the consumer has no idea how expensive the right to tape will become because the difference in price between encoded and unencoded software may be manipulated by the record companies over time. If more and more consumers buy decoder chip recorders, the record companies will be able, by adjusting the pricing differential between the two tiers of software, to make home taping so expensive that the home taping copyright "exemption" of S. 1739 will be a nullity.

Third, the would-be home taper must forecast the future of software, and predict whether record companies will produce an adequate supply of unencoded records, tapes, and CDs. These decisions will be confusing to consumers and enormously burdensome for audio retailers, who will need to help their customers in making these necessary, though complicated, purchasing determinations.

Not just hardware retailers, however, will bear the brunt of the decoder chip provision of S. 1739. Retailers of prerecorded music will be forced to carry titles in six formats -- both encoded and unencoded versions of records, tapes, and CDs. Their inventories will be doubled, and they will be forced by physical and economic constraints to reduce the number of titles they stock. The most likely result is to harm further the less well-known artists -- those whose albums will be squeezed off the shelves when retailers will be forced to stock only the most popular artists. In short, struggling artists will be sacrificed so that the works of the superstars can be carried in all formats. Thus, the only certain consequence of the decoder chip "solution" will be the exact opposite of what the recording industry says it intends by urging enactment of S. 1739.

4. The Proposed Exemption By Class Of User Would Be Unfair To Many Users, Complex To Administer, And Create Substantial Incentives For Evading The Royalty Tax

S. 1739 proposes to exempt users by "class" -- an approach that would, potentially, apply to a wider group than an exemption based on the type of recorder. The user-based classification scheme, however, would arbitrarily exclude many purchases and purchasers that deserve to be exempt, and would be fraught with the greatest administrative complexity.

a. The Definitions Of Exempt Users Are Imprecise, Unfair, And Unworkable

Under S. 1739, businesses able to deduct the cost of recorders as an "ordinary and necessary business expense" under Section 162 of the Internal Revenue Code, or able to take a depreciation allowance for them under Section

167, would not have to pay the royalty tax. This provision is presumably aimed at freeing many business users of recorders from the tax.[153] Many other business users of recording devices, however, would still have to pay the tax. Although Section 212 ordinarily permits deductions for costs incurred by taxpayers in their pursuit of a wide range of investment, property management, and other activities that have a profit-seeking purpose, the proposal would not exempt recorders used for such purposes from the royalty tax.[154] This omission would discriminate unfairly against a large class of users of taping technology who do not engage in "home" taping.[155]

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[153] The bill also appears to extend the corporate exemption to non-profit organizations, presumably intended to help hospitals, foundations, and groups that produce "talking books" for the blind. How the exemption would work, in practice, for such organizations is somewhat confused. S. 1739 exempts recorders purchased either as an ordinary and necessary business expense under Section 162, or as an allowance for depreciation under Section 167, "or, in the case of purchases by a non-profit organization, would be so deductible if neither of those sections were applicable." As neither section _is_ applicable to non-profits, and neither business expenses nor depreciation could be deducted without applying those sections, the meaning of this clause is murky.

[154] Section 212 of the Internal Revenue Code permits individuals to deduct "ordinary and necessary business expenses for the production or collection of income" -- profit-seeking activities, such as investing in the stock market or managing rental property part-time, which do not rise to the level of a full-fledged business covered by Section 162.

b. Administering The "Exemption" Scheme Would Be Costly And An Administrative Nightmare

Under S. 1739, manufacturers and importers would be responsible for paying the royalties to the Register of Copyrights for deposit in the U.S. Treasury. Price increases resulting from the tax would be passed along to the distributors who would, in turn, pass them along to wholesalers and retailers. Many small businesses, their number reaching into the millions, ostensibly would be able to claim deductions under Internal Revenue Code Sections 162 or 167 when they purchase recorders from retail stores. Thus, the exemption scheme would have to be capable of handling such purchases.[156]

A retailer of equipment, faced with a customer claiming an exemption, would first need to assess the validity of the claim. This task, in itself, would prove difficult.[157] Even the simplest of verification systems would generate a flood of paperwork, given that approximately 10,000,000 portable tape recorders were sold in the United States in 1985, with a very substantial percentage being bought by businesses.[158]

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[155] Of course, by shrinking the pool of those subject to the tax, the Section 162 exemption would magnify even further the inequity of the burden on home tapers who do not record copyrighted music.

[156] In 1982, there were four million business establishments in the United States with twenty employees or fewer, out of a total of 4.6 million business establishments. Statistical Abstract of the United States, 1985, Table 873.

Assuming that the retailer can comply with whatever verification system can be devised to assure that only qualified persons receive the exemption, another set of administrative problems is raised by having to maintain separate accounts for taxed and untaxed sales. Three basic systems are possible.

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[157] For example, the following questions would arise: Would the customer's signed affirmation of entitlement to an exemption suffice to qualify for an exemption? (Self-certification would greatly simplify the granting of exemptions, but would lend itself to abuse.) Would the customer have to produce last year's tax return to demonstrate that a Section 162 or 167 deduction had been taken, at least for the previous year? (This would, of course, not necessarily be a reliable indication of the current year's tax status, and would require the retailer to understand and verify the tax returns of many customers.) Or, to assure some uniformity of treatment, would the customer have to file with the Register for a certificate of exempt status in advance of purchase? (This procedure would at least remove from the seller the burden of verifying the purchaser's credentials, but would be prohibitively cumbersome.)

[158] "Consumer Electronics U.S. Sales by Product Category," Table 25 (Jan. 1986).

First, manufacturers and importers could increase the price of every recorder they sell by the amount of the tax.[159] A customer qualifying for the exemption would pay the retail price, less the amount of the tax. For such purchases, retailers would, to recover the tax they (but not the customer) have already paid, be required to forward appropriate requests for reimbursement back up the distribution chain.[160] This procedure would be time-consuming and expensive, given the many points of sale that characterize the market for audio recording equipment. Retailers would have incentives to grant exemptions freely to boost sales, or to file claims with manufacturers and importers for reimbursements for exemptions when such reimbursements would not be merited.

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[159] This increase would be passed down the distribution chain and be reflected in what retailers and wholesalers had to pay for the items and what they charged for them.

[160] The manufacturers and importers would ultimately collect these requests and make reimbursement back down the distribution chain, decreasing by a corresponding amount their subsequent payments into the tax pool. (The manufacturers and importers would, of course, already have paid a royalty for the products for which reimbursement was being sought.)

The second system would be identical to the first, except that qualified buyers would pay the full, taxed price and would apply directly to the Copyright Royalty Tribunal for a refund, instead of being exempted from the taxed price at the point of sale.[161] This scheme would simplify distribution and accounting for all those involved in selling recording equipment, but would obviously create a considerable administrative burden of its own that would, in government, perhaps only be rivaled by the Internal Revenue Service.[162]

Under the third system, manufacturers and importers would release into distribution two kinds of recorders --

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[161] A variant of this system would create a central clearinghouse operated by all manufacturers and importers to administer the refunds.

[162] Customers claiming an exemption would have to fill out a form, provide proof of eligibility, and wait until a distant body processed the application. The refunding body would have to be capable of verifying the authenticity of -- and refunding -- several million separate transactions each year. Some forum for handling appeal from purchasers denied exemptions would be required. It is no understatement to suggest that the whole procedure would be irritating to consumers.

taxed and untaxed.[163] Maintaining duplicate distribution streams of taxed and untaxed merchandise would, however, be complex, expensive, and offer manifold opportunities for abusa.[164]

In fact, all three exemption systems present administrative problems and costs that would far outweigh any gain derived from them. These problems and costs are unavoidable when the products to be taxed are as widely sold as recorders. The scheme of S. 1739 would only intensify these difficulties. It would base the exemption on criteria, borrowed from the Internal Revenue Code, which would not be readily discernible at point of sale. It would assign responsibility for paying the royalty tax to manufacturers and importers, while

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163The taxed products would bear a government seal or stamp. Wholesalers and retailers would pay for and sell the two kinds at two different prices. Consequently, no complex accounting would be required to balance tax receipts at the retail level with tax payments to the royalty fund; as soon as manufacturers and importers shipped taxed merchandise, they would know how much they owed. Upon producing appropriate validation of their exempt status, purchasers would be entitled to buy the exempt goods at the point of sale.

164Retailers would have incentives to sell untaxed merchandise to customers not deserving of the exemption. Pirate manufacturers and unscrupulous distributors, wholesalers and retailers would have a strong incentive to pass off untaxed merchandise as taxed, and pocket the price differential.

assigning responsibility for granting the exemption to the last seller in the distribution chain, or alternatively (in the case of the second scheme discussed above) to a central refunding body removed in time, distance, and first-hand knowledge from the sale for which the exemption is sought.[165]

In sum, the exemption system proposed in the Home Audio Recording Act is plainly unworkable. It would be expensive, unfair to many excluded from the eligibility criteria for the exemptions, an administrative Pandora's Box, and would present substantial problems of enforcement.[166] Yet, forcing consumers to pay hundreds of millions of dollars annually in new royalty taxes without providing for an exemption mechanism would be manifestly unfair.[167] The only solution is no tax at all.

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[165] All three schemes would present opportunities for circumventing the statute, and would require regular policing, either by the federal government or a private enforcement agency of the royalty fund. This enforcement agency would need to have authority to police the entire industry sector. Unquestionably, enforcing the exemption scheme would be costly.

[166] Given the absence of any prior tax on audio products, the public is not likely to be adverse to attempts at evading the royalty tax. Nor is it likely to be favorably disposed to supporting the sizable law enforcement effort that would be necessary to account for the flow of taxed and untaxed recorders, and to catch and prosecute violators.

D. The CRT Distribution Mechanism Will Be Cumbersome And Inefficient

The mechanism for distributing funds is fundamentally flawed because the CRT, the agency with the responsibility for disbursing the royalty proceeds to copyright owners, is beset with problems. Critics of the CRT have singled out its lack of expertise and continuity in calling for its abolition. Even though an attempt has been made in the amended version of S. 1739 to limit the CRT's authority by setting percentages for distribution of the royalty tax proceeds, the CRT is still vested with enormous discretionary power to disburse monies among claimants. To entrust yet another responsibility to the CRT when elsewhere there are vigorous attempts to diminish its authority or to eliminate it entirely demonstrates the folly of the proposal.

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[167] Otherwise, every purchase of recording equipment for the home would be taxed. Also taxed would be businesses whenever an executive bought a recorder to use as a dictating machine; hospitals whenever they purchased audio equipment to record operating room conversations; and educational and charitable groups whenever they acquired a recorder to create a consumer education tape or a talking book for the blind. To be fair, exemptions would have to cover all such purchases of recorders. Even the more limited, less fair ones proposed in this bill, however, cannot be made to work.

The distribution procedure gives prominent play to claimant negotiations that might culminate in a voluntary agreement regarding the distribution of the royalty fees. Such agreement is nothing more than wishful thinking. Nevertheless, if copyright owners do not agree as to what each should receive, they will find themselves litigating before the CRT in a proceeding that is bound to be lengthy and intrusive.

1. The Copyright Owners Are Unlikely To Reach A Consensus About Distribution

S. 1739 encourages owners of copyrights in musical works and sound recordings to reach a consensus about the distribution of the royalty proceeds.[168] Failing such a consensus, the CRT would determine that a controversy exists concerning the distribution of the fees and would be required to conduct a proceeding under chapter 8 of the Copyright Act. Nevertheless, the number of claimants involved[169], the absence of any agreed methodology for measuring the amount of home taping either in the aggregate or for particular songs,[170] the near impossibility of applying the formula that is to guide the distribution process, and the consistently contentious character of other proceedings before the CRT all leave little room for optimism that the claimants would or could resolve their differences expeditiously.

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[168] As mutual agreement is the only way claimants can receive payments without enduring the lengthy CRT-cum-judicial review process, the incentive to agree is strong.

[169] The number of potential claimants is very large. The bill says that "every person claiming to be entitled to royalty fees" may file to receive part of the distribution. Entitlement hinges on whether a copyrighted work was broadcast or included in a phonorecord distributed to the public during the relevant royalty collection period. Over 20,000 published musical works are copyrighted each year, as are over 10,000 published sound recordings. Copyright

Consensus has consistently eluded claimants before the CRT. Established by the 1976 Copyright Act, the CRT now oversees the distribution of compulsory license proceeds from mechanical royalties, from jukeboxes, and from the retransmission of television signals by cable operators. Five of its six royalty distributions have been appealed. The 1983 $80 million cable distribution alone consumed fifty-three CRT hearing days in 1985.

[footnote continued]

Office, Library of Congress. There are, therefore, several hundred thousand copyrighted works for which there could be claims under S. 1739.

[170] Existing mechanisms for distributing performance royalties to the owners of copyrights in musical works -- ASCAP or BMI -- are based on surveys of music broadcast or otherwise publicly performed. Their methodologies could not be adapted because the amended version of S. 1739 requires that radio transmissions or phonorecord distributions of a work be adjusted to the extent that such transmissions or distributions resulted in the "making of audio recordings of musical works or sound recordings by individuals for private use."

Elaborate legal and economic analyses, a long parade of witnesses, and rebuttals of opponents' arguments are presented by each party. Although some claimants do work out voluntary agreements, disputes always remain; they are, given the size of the funds, inevitable.[171]

The same sort of disputes are likely to arise under the amended version of S. 1739 because the proposal requires that the CRT 1) measure the demand for musical works and sound recordings through radio transmissions and distribution of phonorecords; 2) adjust such demand by the making of home audio recordings; 3) adjust the number of phonorecords by price; and 4) adjust the radio transmissions of musical works and sound recordings to reflect the size of the listening audience. Suffice it to say that the CRT will be overwhelmed by the enormously complicated determinations that will be required for two funds and for each of the thousands of copyrighted works that are bought, broadcast, and taped each year.[172]

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[171] S. 1739 seeks to mitigate concerns about administrative delay by providing for distribution of funds that are not in dispute. It states that the CRT, while a distribution proceeding is pending, "shall have discretion to proceed to distribute any amounts that are not in controversy." Although the provision is designed to encourage voluntary agreement among claimants, it would be difficult to achieve in practice. As the royalty funds are finite, any dispute about the share a claimant deserves would affect the shares of all other claimants. The CRT may be able to disburse proceeds where the amount in controversy is essentially de minimis. See, e.g., National Ass'n of Broadcasters v. CRT, 772 F.2d 922, 939 (D.C. Cir. 1985) (settlement possible where unsettled claims total less than 10%). It is likely, however, that the multiplicity of claims to the Sound Recording and Musical Work Funds would make such disbursal nearly impossible. For example, if the sum of all the claims in the Sound Recording Fund were to exceed 100%, which is customary in proceedings such as the one contemplated by the bill, how can the CRT know whether the three parties who may have agreed among themselves how to divide up 50% of the pool actually deserve 20%? Put succinctly, the relative shares of all parties cannot be fixed until the whole structure has been determined.

The proposal requires the CRT to measure home taping, to ensure that copyright owners will be compensated for actual home taping. In practice it will be difficult, at best, to obtain these data.[173] Thus, it is probable that only surrogate measures for the incidence of home taping of the thousands of copyrighted works released annually will be available.[174] Despite the great difficulty of collecting the necessary information, the fundamental purposes of the copyright law demand that there be a correlation between compensation and the works being taped. Thus, as it seems probable that payments to copyright owners necessarily will be based on imprecise or incomplete data as to what people are taping at home, the rationale of the recording industry proposal will be severely undercut.

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[172] The adjustment of demand for phonorecords by album "price category" is entirely counter-intuitive. The demand for an album is measured by the number of units sold, not by a dollar amount. Although the intent of S. 1739 appears to be to compensate copyright owners for lost sales of taped music, the statutory scheme would, in fact, grossly overcompensate the record companies and songwriters. The retail price of an album does not accurately reflect the amount of net income "lost" by a displaced sale because that price includes the manufacturer's cost, and wholesale and retail markups. In any event, by requiring that the CRT multiply demand by price, S. 1739 provides enormous incentives for manufacturers to raise the price of a title to increase the size of the claim for compensation for the taping of that title.

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[173] First, given the various measures necessary to estimate what is being taped at home, and how much, collection of the relevant data will take time. Moreover, claimants will inevitably complicate the process of reaching agreement by stressing the measures most favorable to their own claims, taking advantage of what are likely to be serious disparities in information-gathering resources and bargaining power between the larger companies, and smaller companies and individuals. These disparities virtually guarantee that the proceeds will not be distributed to aspiring young musical artists, but will enrich established companies.

[174] Such measures might include sales of singles, sales of albums, sales of tapes and compact discs, radio and television broadcast frequency, surveys of home tape collections, statistics about press coverage and live concerts, and other data that could have a bearing on home taping frequency. The stimulative effect of home taping on sales of prerecorded music will also be relevant.

2. The Process Of Distributing Royalties Will Not Serve As An Incentive To Creativity

Although there have been some voluntary agreements among claimants before the CRT in the past, the large number of potential claimants eligible to file under the amended version of S. 1739 makes it probable that distribution among them will be enormously difficult and time-consuming. Long-term litigation before the CRT is commonplace. Indeed, the U.S. Court of Appeals for the District of Columbia Circuit recently described the "copyright-owner subculture" as "highly litigious" in adopting a "litigation-to-the-hilt" tack.[175] Delay, in short, is inevitable.

The lapse of time between a home taping event and the receipt of "compensation" therefrom (assuming that it were possible to make a correlation between the two) will cause substantial uncertainty for record companies and composers and lyricists. Thus, they will not readily be able to rely on compensation from the royalty funds in evaluating the profitability of or demand for particular artists or kinds of music. Hence, contrary to the purposes of the copyright law and the purported rationale of S. 1739, the proceeds from the royalty taxes will not serve as an incentive for the creation of the copyrighted works that the public wants.

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[175] National Ass'n of Broadcasters v. CRT, 772 F.2d at 940.

Further distorting the incentives for creativity is the proposed concept of the Incentive Class, which include the works for which demand was in the lowest 30%. Incentive Class claimants will be allocated 20% of the Sound Recording and Musical Work Funds. The copyright law, however, is based on the notion that the flow of works to the public is and should be dependent on the public's interest in such works, as measured by its willingness to pay for them. Consequently, by funneling consumer dollars to the less popular artists, those whose works are probably least taped, S. 1739 unabashedly departs from its stated premise of affording "compensation" to copyright owners in accordance with the extent to which their works are taped.

3. The Copyright Royalty Tribunal Is Incapable Of Performing Adequately

The CRT, charged with distributing the proceeds of an audio royalty tax when the claimants to the two funds are unable to reach a consensus, will face a multitude of parties raising complex legal and economic issues.[176] The CRT is now in danger of being disbanded due to its inadequate staffing, its disorganization, the qualifications of its members, its lethargy, and its approach to the tasks with which it is charged under the copyright law.[177] The CRT has performed so slowly and incompetently that two bills were introduced in the last session of this Congress to overhaul it.[178] The experience to date with the CRT has shown, repeatedly and consistently, that it simply does not have the continuity, expertise, and coherence to perform the distribution function.

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[176] How, for example, will the CRT -- or, indeed, any organization -- be able to resolve as complex an issue as the demand for sound recordings made by musicians and vocalists not represented by the unions, which S. 1739 requires for distribution of the Musician and Vocalist Fund?

[177] That the CRT's resources are inadequate has been the subject of much judicial notice in the context of the repeated appellate proceedings that have challenged the Tribunal's determinations. See National Ass'n of Broadcasters v. CRT, 772 F.2d at 929 n.9; Christian Broadcasting Network, Inc. v. CRT, 720 F.2d 1245, 1304 (D.C. Cir. 1983); National Cable Television Ass'n v. CRT, 689 F.2d 1077, 1087 n.74 (D.C. Cir. 1982).

[178] H.R. 2784, introduced by Rep. Robert Kastenmeier, would establish a new federal Copyright Royalty Court composed of three sitting federal judges appointed for six-year terms, and give it support staff, clerks, and a general counsel. Competing parties would first be required to negotiate among themselves, and to accept intervention from a court-appointed mediator if necessary. If voluntary agreement were not reached, however, the bill is aimed at ensuring that the new court would have expertise both in methodical evidence-gathering procedures and in the substantive law and economics of royalty distributions.
H.R. 2752, introduced by Reps. Patricia Schroeder and Mike Synar, would abolish the CRT immediately and transfer its duties to the Register pending a more thorough reform.

4. The Scheme For Adjusting The Amount Of The Levy And Disbursing The Proceeds Is Constitutionally Infirm

S. 1739 is constitutionally flawed because it requires that, after five years, and at five-year intervals thereafter, the CRT adjust the amount of the levy, as well as disburse the proceeds from the royalty tax. Performing these functions involves adjudicating interests between private parties -- copyright owner claimants, on the one hand, and manufacturers and importers, on the other. Recent decisions of the Supreme Court suggest that these tasks, involving essentially private rights, should be undertaken by federal courts, created by Congress pursuant to Article III of the Constitution, and not by entities created pursuant to an exercise of Article I powers.[179] Thus, the framework of S. 1739 raises significant constitutional questions that could require post hoc resolution by the Congress, much like the way in which it had to grapple with the unconstitutionality of the bankruptcy courts.

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[179] See Thomas v. Union Carbide Agricultural Prods., Co., 105 S. Ct. 3325 (1985); Northern Pipeline Construction Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982).

E. S. 1739 Is Based On An Unduly Expanded Concept Of Contributory Infringement That Makes Equipment Manufacturers Liable For Home Taping

S. 1739 purports to exempt consumers from copyright liability at the same time as it imposes a tax on them. This is legislative legerdemain that will not pass close public scrutiny. The recording industry claims that suppliers of tape recorders are and should be liable for the ultimate use to which end users put those devices. Nevertheless, even if Congress were to repeal the rights established under the 1971 Act and accept the recording industry argument that home taping is an infringement of copyright, it would still not be legitimate to ascribe liability for that infringement to manufacturers and importers of recorders, either as an equitable principle or pursuant to the law of copyright as interpreted by the Supreme Court. Consequently, S. 1739 may set a dangerous legislative precedent by broadening the liability of manufacturers for the public's use of their products.[180]

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[180] Car manufacturers, for example, are not, and should not be, held liable because some purchaser of their products may use them to escape after bank robberies, or because virtually every car has the capacity to exceed 55 miles per hour, or because advertising for sports cars extols their speed. Photocopier manufacturers are not, and should not be, held liable because some users may use high-quality reproductions to perpetrate a fraud. There is no principled reason

The amended version of S. 1739 purportedly exempts from contributory liability entities that import, manufacture, or distribute audio recording media, or licensed importers, manufacturers, or distributors of audio recorders. Nevertheless, the bill expressly makes such manufacturers and importers liable for home taping -- a liability that the law does not now impose and one that is contrary to the holding in Sony.[181]

[footnote continued]

to single out the electronics industry as incurring liability based on the activities of end users.

[181] In reviewing the bill, the Congress should look to the Sony decision for guidance in deciding whether to enact a new standard for contributory infringement. In Sony, the Supreme Court directly considered whether equipment manufacturers should be considered contributory infringers because the public engages in home taping activities. The Court concluded that "the sale of copying equipment, like the sale of other articles of commerce, does not constitute contributory infringement if the product is widely used for legitimate, unobjectionable purposes. Indeed, it need merely be capable of substantial noninfringing uses." [emphasis added] 104 S. Ct. at 789. The remarkable variety of completely unobjectionable uses to which recorders are put -- recording dictation, press conferences, piano recitals, and birthday parties, and storing home computer programs -- leaves no doubt that they are "capable" of substantial non-infringing uses. The rationale of Sony, therefore, would preclude a conclusion that home audio taping practices should make equipment suppliers liable to copyright owners.

By distorting technology, by creating incentives for certain equipment configurations that would not otherwise be developed apart from a royalty tax, and by subordinating the electronics industry to the recording industry, S. 1739 will unwarrantedly intervene in the future product development and marketing strategies of consumer electronics of the United States. Both the electronics and recording industries are enjoying success and, most important, present the American consumer with an unparalleled array of choice in hardware and prerecorded music. S. 1739, therefore, represents an unnecessary --and harmful -- intrusion into a now healthy market. For that reason alone, Congress should decisively reject the royalty tax proposal.

Senator HEFLIN. Do you have any questions?

Senator DECONCINI. Yes.

Senator HEFLIN. Go ahead.

Senator DECONCINI. Mr. Gortikov, if S. 1739 should pass the Congress and be signed by the President in its present form, would your member recording companies begin encoding their software in accordance with the decoder chip provision, or would they wait to see what the manufacturers and the consuming public wanted?

Mr. GORTIKOV. There would certainly have to be some—the advantage of the decoder system is that is does respond to the marketplace. If there is a demand for——

Senator DECONCINI. You would wait, then?

Mr. GORTIKOV. Yes.

Senator DECONCINI. Yes.

Mr. GORTIKOV. But there is a distinct chance with DAT coming on that a different practice may have to be invoked of prompt encoding.

Senator DECONCINI. If your members do encode their products in accordance with the provisions of this bill if it became law, what would be the price differential between the encoded and the unencoded software?

Mr. GORTIKOV. That is totally unknown, Senator. This would—again, the beauty of this is that the marketplace would determine through supply and demand if there even is a price difference and what it would be.

Some companies, for example, might choose to not encode, and there would be no control over the price any more than there is for any other optional products that are available in a drugstore or in a market or in any other place right now, or even on blank tape right now.

Senator DECONCINI. You have not had discussions with your members about what the cost entailed might be?

Mr. GORTIKOV. No, sir. That would be totally inappropriate legally, anyway.

Senator DECONCINI. Why would it be inappropriate? Would not good, prudent businesses think about the future if such a bill were passed; that at least someone would be thinking about what the cost would be and what the market might bear?

Mr. GORTIKOV. I am not saying that companies individually might not be thinking of what their relative prices might be. But, certainly, in aggregate, we are not studying what pricing differentials or practices might be. That would be for the marketplace to determine.

Senator DECONCINI. Mr. Ferris, I have not been a supporter of this bill for a long time, but I do see that the amendment has made some improvements. There is no tax on tape in this proposal, something that we both have objected to for a long time.

The mechanism to allow a nontaper to avoid the fee on a machine is provided here. What concerns me is there is some case made that merely supporting vigorous enforcement of the present law would cost money, like you say this is going to cost money.

It is going to cost the consumer one way or the other—higher taxes, higher Government enforcement. I think your clients' position has been well argued here, particularly as to the no tax on the tape.

Do you have any other suggestions, other than just being against it? I am going to try to be a solution solver rather than just in opposition to something. Is there anything that your interests can support, in addition to no tax on the tape, to cope with the particular problem?

I do not see it quite as simply as you do. You just see the right of myself to go home and create my own 90-minute tape. What I do see some people doing is buying a tape and wanting to be able to play it in the office, at home, and in their car.

So they buy one at the market price and then make three copies, and maybe they give one to their brother-in-law as a present. Then they get the use of this without any additional royalty to the people who deserve it.

It does not really trouble me that they use it for themselves, but I wonder if you have given any thought to how far you expand this. What if you give it away for presents, if you make these tapes and give them away to everybody in your office?

You buy the latest Bruce Spingsteen record and record it on a tape and then you give a copy to your executives, and that saves you money. What about that type of abuse?

Mr. FERRIS. Well, Senator, addressing the first part of your question about what recommendations we should have, I think time and reflection is probably the best remedy because if you look at the history of this issue as it has gestated before Congress, 4 or 5 years ago we had the same issue of royalty taxes on machines and tapes not only directed to audio home taping, but to video home taping as well.

In this Congress, there is no bill that addresses video home taping. And the argument and scenario that we provided this committee 4 years ago—that the video cassette recorder was the best friend that Hollywood ever had—has proven to be valid. Today, the most significant revenue stream for Hollywood studios is the sale of its prerecorded video cassettes for use in the VCR's. Four years ago, those Hollywood studios were convinced that VCR's were going to destroy theaters and were going to destroy watching commercials, thus undermining their products' desirability on commercial TV.

The same thing has happened as this bill goes through its gestation period. First, the elimination of blank tapes from the taxation of this bill. Now, the tax on audio machines has been eliminated by the administration in their testimony today because they will not support such a tax.

Senator DECONCINI. I will not either.

Mr. FERRIS. What I wish to stress again is the remedy is what everyone has been focusing on rather than what is the real harmful activity involved in home taping.

Now, on the second part of your question about making a tape, I buy a record and make a tape and I give it to my friend. I think the copyright law has always made a distinction, and rightly so, between commercial uses—of copying for profit—and copying for personal use.

I can make a copy of a book and give it away, and that is valid under the copyright law. It is not economically a wise thing to do because Xerox charges are so significant, but that is not a violation of the copyright law.

I cannot sell it, but I can replace my personal copy without any copyright liability.

Senator **DeConcini**. Do you not see a big difference between a tape, not only as to the cost but as to the compactness, of giving a tape of a popular record versus trying to Xerox Leon Uris' "Trinity" and giving that to your brother-in-law or to your relative?

You know, practically speaking, you are not talking about the same thing. What I am concerned about here is that I think you should have the right to duplicate it for your own use; I really do.

I do not feel sorry for the industry or the recorders. That is part of the business. By you playing the tape, the record is going to be more popular. But what if you do reproduce it and give it away? Is there not some line that that goes too far, in your judgment?

Mr. **Ferris**. Yes.

Senator **DeConcini**. What do you do about it?

Mr. **Ferris**. I think the line should be drawn at hoping for commercial gain. I think that Congress at the outset should determine what is the ordinary and accepted human behavior from the standpoint of the borrowing and lending of goods, and whether Congress should inject itself and burden that particular process by legislation.

I think that is probably why the historical judgment of the Congress has been to draw the line at commercial gain. But you should not start restricting the normal social behavior of exchange of goods that are owned by a person. When I buy a copyrighted work, the copyright law is rather established that I own that and I have rights to that copy.

The copyright holder, when he issues that copy and authorizes copies to be made, gives me that right. And I think I should have the right to use that in the normal course of social behavior, and that includes borrowing it and lending it to my friends.

Senator **DeConcini**. But that is different than duplicating it and giving it to all your relatives, say. Is that a proper thing, in your judgment?

Mr. **Ferris**. Well, first of all, I think it is proper, Senator.

Senator **DeConcini**. Let me give you a hypothetical.

Mr. **Ferris**. Yes.

Senator **DeConcini**. I have got a lot of relatives in Arizona and a lot of them are under the age of 22, my nephews and nieces. And I buy the latest hit record, I record it, and I want to give it to them all. Of course, that saves me buying them that record for Christmas, graduation, what have you.

In your judgment and standard, that should be permissible?

Mr. **Ferris**. Yes, I think it should be; I think very definitely it should be. I think implicit in that, one could come to the fallacious conclusion that you, if you did not copy that, would purchase a copy and give it.

Senator **DeConcini**. That is right.

Mr. **Ferris**. I think that that probably—in your case, I certainly do not question the fact that you would do that, Senator, but I think in many cases people would not purchase copies and make gifts of them.

But I think all of this dynamic and all the anecdotes one can conjure up with respect to giving tapes away and kids copying tapes should be put it in perspective. How much of the total dynamic of recording is involved in that?

Senator **DeConcini**. That is a good question, and I do not think we know and I suspect it is greatly exaggerated.

Mr. **Ferris**. It is greatly exaggerated.

Senator **DeConcini**. But we do not know.

Mr. **Ferris**. Well, if we look in the record below, Senator, the Yankelovich study and the studies by the recording industry do address that particular question. And of all the recordings that take place with all these machines, over 50 percent have nothing to do with copyrighted work at all.

Over 50 percent of all recording events have nothing to do with copyrighted works. So, of the less than 50 percent that do have something to do with music, a majority of that is of the individual who purchased the music making a copy for his Walkman, for his car, or whatever.

And so I think that when you make it for your own personal use—in your structuring of the question, you said that that does not bother you at all.

Senator **DeConcini**. It does not bother me.

Mr. **Ferris**. So we have already gotten rid of 75 percent—over 75 percent of all the recording events should trouble you not at all. Then part of the remaining 25 percent are the kids primarily who are going to be taping from the radio, listening to the radio and making a tape from the radio. So they are not going to purchase anything; they are going to tape it.

That activity, under the Sound Recording Act of 1971, was very explicitly stated to be lawful under the copyright law. So we are getting down to a very small segment of the events which everyone is intrigued by.

I imagine regardless of where you come out on that spectrum, Senator, as I say, I think you should be able to make copies and give them to friends if there is no commercial gain.

But even if you have a more restrictive view than I have on that, the number of events that you are really concerned with is insignificant when you consider putting a tax of a significant amount on all of this audio equipment. The recording events of concern are such an overwhelmingly small part of the spectrum of uses of this equipment. And let me reemphasize, it is not for commercial gain.

Senator **DeConcini**. Well, if your mathematics are correct, you make a pretty good argument. Let me ask you this; let me carry it one step further. What if I have a company and I have 40 employees and I decide to buy "White Christmas" by Bing Crosby and I decide to tape it, wrap it up and give it to all my employees as a Christmas present?

Do you think that is going too far in the area of gifts, being able to do it for your own use?

Mr. **Ferris**. Well, I imagine at some point you are going to say it is an act of piracy and I would agree. What you are doing is you are in the business of pumping out "White Christmas" and you are getting some gain from that, for that use is one of a commercial nature.

And I think if, in your business, you normally buy gifts and give them to your employees and this taping would replace it, I think you could make a good case that this crosses the bridge to commercial activity.

Senator DECONCINI. I think you could, too. Let us assume that we both agree that there is a line where it becomes nonpersonal use and gifts. What do you try to do, if anything, to prohibit that? Through present enforcement, can that be done?

Mr. FERRIS. On gifts?

Senator DECONCINI. Yes.

Mr. FERRIS. I think the line that Congress has historically drawn between commercial gain and personal use is probably the only defensible, enforceable line that can be drawn.

I think when you attempt to invade the ordinary and accepted human conduct of the exchange of goods when there is no commercial gain involved or a substitute for commercial gain involved, I think then you get on the slippery slope——

Senator DECONCINI. Then it is piracy and subject——

Mr. FERRIS. I think the line has wisely been piracy and nonpiracy. I think that is what it comes down to.

Senator DECONCINI. Well, if you give it to your relatives, it is nonpiracy. If you have 400 employees and you decide to buy one tape and record it all and give it to them, and thereby you do not have to buy them a present or a bonus at Christmastime, that is piracy, right?

Mr. FERRIS. I think you could make a valid distinction between the two because I think one might be a substitution for a purchase that would certainly save your company——

Senator DECONCINI. Money.

Mr. FERRIS [continuing]. Money.

Senator DECONCINI. Thank you. I have no more questions. Thank you, Mr. Chairman.

Senator HEFLIN. Senator Denton, do you have some questions?

Senator DENTON. Not at this time.

Senator HEFLIN. I was presiding in the absence of the chairman, who has gone to open the Senate, but I would be delighted for the Republican Party to take over the responsibility of chairing. [Laughter.]

Senator DENTON. I appreciate the acting chairman's offer; however, I would request that you permit me to go to a brief meeting that I had previously scheduled. I do have interest in this, however.

Senator HEFLIN. Do you have some questions?

Senator DENTON. No sir, not at this point.

Senator HEFLIN. All right.

Both of you might answer this. Today, Commissioner Quigg testified that the administration recommended that the encoder chip technology be used. What is your opinion on this proposal?

Mr. GORTIKOV. Well, the decoder chip technology, we heartily favor. We certainly think that it is an answer to the eventual digital audiotape equipment emergence. We think, however, that it will be many decades, even if invoked right today, before it can significantly impact the practice of home taping.

This is why we feel that transitionally, S. 1739's incorporation of a royalty provision is an essential until decoder technology can meaningfully impact home taping.

Mr. **Ferris**. Senator, I think that we certainly welcome Mr. Quigg's testimony because it definitely did not support the royalty tax on equipment. So I think each whittling away of this present bill is a very welcome recommendation to us.

I think the recommendation was less precise, however, in talking about working with the Congress and working toward a solution. It raises again the question of really fashioning a remedy. I do not think one can do that until you really make some very basic findings as to what the rights of the parties are; to truly define what is the problem that needs to be addressed.

I think the chip technology has significant ramifications from the standpoint of the marketing of equipment. I think the question that was addressed to Mr. Gortikov by Senator DeConcini about the price differentials between the encoded and unencoded software demonstrates the complexity of the approach—and unless you are going to proscribe what the differential will be, you are permitting the copyright fee to be determined solely by the recording industry.

Thus, they will determine whether you can home tape or not and if they permit it, what premium you are going to pay. I think the remedy of this bill, even as it seems to be narrowing down to a chip bill, is riddled with problems that have not been fully thought through.

I am sure that the commissioner and the administration, when they undertake the study that is implicit in their remarks today, will come to conclusions different than probably what they would conclude today, further restricting, I am sure, any recommendation as to what should be done.

Mr. **Gortikov**. Senator, what is ignored here totally is that there even is any kind of a problem. What is ignored here totally is that there is a property right involved; that there is a negative impact on people's careers, lives, and economics. That cannot be ignored any longer.

There is a fairness issue involved here, and this is why we implore serious consideration and not brushing aside of every alternative without offering any other option, and that is why we urge a direct, head-on answer to this through S. 1739.

Mr. **Ferris**. Mr. Chairman, may I submit for the record later this week a paper that we have drafted defending audio recording rights?

The **Chairman**. All right.

Mr. **Ferris**. Thank you.

The **Chairman**. How much do you estimate the royalty tax on tape and tape equipment would raise, Mr. Gortikov?

Mr. **Gortikov**. Well, it is not a tax, Senator, because it does not go to government—it is a royalty that goes to creators and rightsowners. It is estimated that it would yield approximately $100 million applied on equipment alone.

The CHAIRMAN. It has been stated that some consumers use taping equipment to make copies of records they have purchased in order to preserve them or so that they may have an extra copy for their car or Walkman.

Do you feel that this kind of taping behavior is unjust or taking money away from copyright owners?

Mr. GORTIKOV. Well, I certainly feel that a property right has to be respected. For example, if you own a hardcover book and you want another copy in paperback, you have to go out and buy it.

Why should our product be the only product that is replicable for free? If you want another can of coffee, you go and pay for a second can of coffee. Any other product or service that is desired by a consumer in multiples is paid for, and we feel that should be observed with ours, too.

The CHAIRMAN. Under the bill, taping equipment that is capable of making two or more copies at one time is prohibited. How can you justify outlawing such equipment entirely? Is not such equipment used professionally in the recording industry and for educational purposes?

Mr. GORTIKOV. Equipment for professional purposes would be exempt from this. The tribunal would have a right to decide procedures for effecting such exemptions.

The CHAIRMAN. From a procedural aspect, how do you believe that the exemption process would work?

Mr. GORTIKOV. This would have to be developed by regulation and by the tribunal. I think it could be done directly by the manufacturers and importers. It can be worked out; it is not insurmountable.

The CHAIRMAN. Under the bill as proposed, a royalty would be paid on equipment that is capable of recording. However, if the recording has an encoder chip in it, no royalty will have to be paid.

Would the price of a record or tape which can be recorded be affected?

Mr. GORTIKOV. This would be determined by the marketplace. I think Senator Heflin raised this before. It would be determined by the marketplace. If there was demand for price differential in different inventories, this could be effected.

The CHAIRMAN. Would the extra money go to the copyright people?

Mr. GORTIKOV. I could not hear that.

The CHAIRMAN. Would the extra money go to the copyright people?

Mr. GORTIKOV. The money would go to the copyright owners, creators, performers, songwriters, music publishers, and musician and vocalist unions.

The CHAIRMAN. Mr. Ferris, for what purposes is the consumer using taping equipment?

Mr. FERRIS. What purposes?

The CHAIRMAN. Yes.

Mr. FERRIS. I think the record below, Mr. Chairman, demonstrates that people who use recording equipment use tape and their equipment for many, many reasons, the majority of which have nothing to do with recorded music.

Of the minority that is left of uses that do have something to do with prerecorded music, a majority of those recording events, Mr. Chairman, are the taper making a copy of prerecorded music that the taper purchased himself.

It is my view and our coalition's view, Mr. Chairman, that that is activity that is legal and lawful under the present copyright law and should not be declared unlawful, as S. 1739 implicitly does.

The **Chairman**. In your testimony, I believe you stated that the new technology has actually helped the recording industry. Would you elaborate on this?

Mr. **Ferris**. Yes. I think the history of this industry, Mr. Chairman, is very, very interesting. The record before the subcommittee—Mr. Gortikov's testimony and others in the recording industry have testified that the recording industry generally was in very deep trouble in 1979, 1980, 1981, at the turn of this decade.

If you look at the reasons for that trouble, they really have nothing to do with home taping, even though the recording industry felt then that home taping really was causing their problem.

What did happen was that the manufacturers of hardware devised new hi-fidelity equipment that provided portability of music—the Walkman came on stream in 1980–81, and then the boom boxes and the other types of very hi-fidelity stereo in automobiles.

I think the recording industry has finally responded to the new market for prerecorded cassettes. Back in 1980–81, you could get—less than half the titles offered by the recording industry in prerecorded cassette form. Phonograph records, the plastic or vinyl discs, were being distributed more than the prerecorded cassettes by a significant amount.

Today, prerecorded cassettes—a good guide to portability outsells the vinyl disc by almost 3 to 1. I think it demonstrates that the recording industry has been made healthy by the home taping phenomenon. The desire of the individual who buys a phonograph record is to put it on a cassette so they can use it in their car or in their Walkman, and that added dimension has really stimulated significantly the sales in the recording industry, which has given it the record profits it has had in 1984, 1985, and again this year.

Mr. **Gortikov**. Senator, there is some distortion in that comment. Whereas a given record company can have a record profit in a given year, it may not the next year. At the same time, there are many companies that are not making profits at all.

What is overlooked, for example, in the display of this audio equipment here, is that almost every one of these devices is dependent on the creation of copyrighted recorded music, or else it would just be a bunch of chemicals and plastics and wires and chips.

We are seeking a fair response to the rights and the property rights of that core of music that makes all these machines possible.

The **Chairman**. Mr. Ferris, I believe you testified that musicians who use taping equipment to make demonstration tapes would have to pay the royalty on machines. Why would that not be a business expense for which an exemption could be received?

Mr. **Ferris**. Well, the whole exemption process, I think, under this bill is an administrative nightmare, Mr. Chairman. I am sure that you could declare an exemption for any classification under this bill.

This royalty tax, Mr. Chairman, is going to be assessed at the manufacturing level. The manufacturer then is going to sell it to the distributor; the distributor is going to sell it to the retailer, and the retailer is going to sell it to the individual consumer.

Now, if the individual comes into the store and says I am a home musician and I want to buy these tapes because I am going to distribute them so that I can become more widely known or so that some record company might be willing to record my product, the first question you should ask, Mr. Chairman, is what burden of proof will you wish to impose on that retailer as he approaches this potential sale.

Is he going to have to get an affidavit from this customer at that point? And then if he does meet your requirements of proof, or whatever standard that you require, then a refund technique is going to have to go back up the distribution chain. The refund is going to go from the retailer to the distributor, from the distributor to the wholesaler, from the wholesaler to the manufacturer, and then the manufacturer is going to have to go over to the Copyright Royalty Tribunal and seek a rebate.

Just think what happens if the Copyright Royalty Tribunal says we do not think you have got enough evidence and your are going to have to go back down that chain again to get more evidence.

I think you are putting into motion an administrative and bureaucratic nightmare that I really hope this committee will think through before it seriously considers any exemption process, regardless of who should be included in that class.

The CHAIRMAN. Would you care to respond to that?

Mr. GORTIKOV. Yes; I think this is overblown. The amount of royalty that would be charged, when amortized over the total use of the machine for the prolonged life of the machine, would be truly modest. We are talking about a miniscule effect on a consumer.

If there are significant constituencies that have to be exempted, processes can be worked out for that. I promise you the bill and the effect will be imperfect, but Congress is addressing, for example, a tax bill that is also imperfect. But, yet, it is attempting to fashion a response to a greater, grander need.

That is what we are trying to do there, is to get a serious response to a need and not brush it under the table, as Mr. Ferris is attempting to do, as a nonproblem without a property right implication.

The CHAIRMAN. Mr. Ferris, under the bill, taping equipment that is capable of making two or more copies at one time is prohibited. Is this a desirable approach?

Mr. FERRIS. I see no reason why there should be a prohibition at all. I think the multiple-bay equipment is responding to a market need. I think it provides opportunity for sequential play of taping, and I think it provides a very convenient way for duplicate tapes to be made by the purchaser of the prerecorded music, which I think is very acceptable activity, and certainly is lawful under the present coppyright law.

The CHAIRMAN. Would you care to respond?

Mr. GORTIKOV. The multiple-well can be allowed for the uses that are described as totally permissible if it contains a decoder chip that would prevent copying of recorded works.

The CHAIRMAN. I had to go and open the Senate. Did you comment on the position taken by the administration?

Mr. FERRIS. Yes, Mr. Chairman. I certainly welcome the administration because what they said is, in effect, that they do not support S. 1739, as it imposes a royalty tax on equipment. That is very welcome news.

I think they said that they would like to work with the Congress in attempting to devise a technological or chip solution. I think any further study of this is good because I think the history on this bill, Mr. Chairman, is that the more people study, the more they realize that the proposals of this bill and its remedy are so overbroad that it has to be continually restricted.

I am sure the study the administration hopes to give to this will further lead them to make recommendations that will be much more restrictive than at present, and I am sure that they will ultimately conclude as we do that no remedy is required because there is no right here to which a remedy is addressed.

The CHAIRMAN. Did you comment on the administration position?

Mr. GORTIKOV. No, sir; I did not.

The CHAIRMAN. Would you care to do that?

Mr. GORTIKOV. Yes, sir; I would. The administration position in fostering decoder chip over royalty is certainly understandable in the long range. We advanced the royality proposal as an interim solution that is needed now because the decoder technology, once introduced, will require decades before it seriously can impact broadly the home taping problem.

So S. 1739 addresses that. We can study this thing to death while the house burns, and the house is burning, and that is why we urge the royalty solution transitionally until decoder technology can take over.

Mr. FERRIS. If the house is burning, Mr. Chairman, it is burning from profits because the record industry is having the hottest years in their history in 1984 and 1985 and 1986. I see no reason why a new Federal subsidy should be created for such a healthy industry.

Mr. GORTIKOV. But the question of profits is irrelevant here. There is no ceiling put by law on how much any industry or any company can make. What we are talking about here is the penalty on creators and rights-owners.

There is an economic penalty and a deprivation of achieving potential, and that is ignored. Certainly, we are not addressing the profits of the Japanese equipment companies. Perhaps we should.

We are asking for a fair share of their yield to go to the people on whom their products are dependent.

The CHAIRMAN. The distinguished Senator from Arizona.

Senator DECONCINI. I asked my questions, Mr. Chairman. Thank you.

The CHAIRMAN. Thank you both for appearing. You are now excused.

For the next panel, we will ask Mr. John V. Roach, Mr. Jack Eugster, and Mr. Edward Jarman to come around.

Mr. Roach, would you care to make a 5-minute opening statement? You do not have to unless you want to.

STATEMENT OF A PANEL CONSISTING OF JOHN V. ROACH, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, TANDY CORP.; JACK W. EUGSTER, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, MUSICLAND, INC., MINNEAPOLIS, MN; AND EDWARD JARMAN, PEPPERMINT RECORDS AND TAPES, TAYLOR, SC

Mr. **Roach**. I will be glad to. I appreciate the opportunity to make a statement. I represent Tandy Corp. and a number of other electronics manufacturers and retailers.

Tandy makes and sells the end users' business and consumer electronics products. We have over 20 manufacturing plants in the U.S.A., most of them opened in the last 15 years. We employ 27,000 U.S. citizens, sell to over 30 million grassroots American households annually, and are probably the largest third-class mailer in the United States.

We have over 7,000 stores and dealers. The breakdown by States is attached, including 96 stores in South Carolina and 111 stores in Arizona. The retail names we operate under include Radio Shack, VideoConcepts, and McDuff. Radio Shack alone sells 60 different types of audio recorders.

This proposed legislation is going to make serious problems for both manufacturers and retailers. We are opposed because the legislation, in our opinion, is unnecessary, it is unfair, and is absolutely unworkable.

Philosophically, it is bad because millions and millions of recorders are used for absolutely legitimate purposes. Congress should not give an unwarranted boost to the recording companies and their superstars at the expense of consumers and the hardware manufacturers who have made their industry possible.

Through continually lower and lower prices made possible through technology, innovation at higher cost, economies of scale, investments in plant and equipment, and hundreds of millions of dollars in advertising, the audio tape recorder has been made affordable to most Americans.

Until the recording industry proves it is getting more harm than good, until it proves it is losing money, then legislation is an unnecessary burden on consumers, manufacturers, and retailers.

Consumer electronics, as you probably recognize, is a very highly competitive business with frequent retail business failures, and the burden of this legislation will be the worst on the independent retailer and the moms-and-pops, and even for some chains it could be the last straw.

The exemption proposed for nonprofit and business users, while probably correct in theory, is highly unadministrable, and there is a lot of confusion that is created by this act just in general.

We have to ask as a retailer, should we sell new or used recorders? Can we sell recorders in combination with anything else, like rack systems or component video systems? Can a unit be designed that has such predominant legitimate uses that it avoids the royalty?

If you look at the ad copy in our brandnew catalog, "desk-top or portable, perfect for dictation or notes, slim style, ideal for students, our best electronic note-taker; cassette recorder with amazing time-saving variable speech control; voice-accentuated cassette recorder."

Yet, every one of those machines is also capable of recording prerecorded music, and particularly if you are smart enough to do it.

Also, obviously, there will be higher prices because the royalties or decoder—they must be marked up at each level of the distribution channel. The case of the decoder is equally unworkable.

We have to decide, do we carry units with and without decoders? Obviously, this would create two additional inventory investments. We have chaos on the sales floor. You cannot imagine how many questions we answer in 1 day from customers about equipment, in general.

Well, customer, yes, we have this unit with decoder which will record old music and new, unencoded music, but will not record new, encoded music, or we have this old unit which will record both old and new music, or you can buy—I do not know; I am confused myself. [Laughter.]

We would be forced to educate the American public on whatever it is we are trying to do. Many machines would be brought in for repair with nothing wrong. This is somewhat of a problem in the industry already; it would just be magnified substantially.

Decoders would hurt the most those people who are least able or willing to pay because the lower the cost of the unit, the greater the impact of the decoder on the price of the unit, and I am talking about price increases of 30 to 50 percent on low-end units.

The royalty tax, as far as we are concerned, is absolutely absurd because it is significantly higher for vertically integrated domestic retailers like Tandy and significantly lower for foreigners and importers.

In some cases, the tax is levied on the manufacturing cost; in some cases, on the retailer's cost; in some cases, on the consumer cost.

Then we have the question, if you are going to have a royalty tax, is the tax charged on list price, advertised price, negotiated price, with or without rebates and allowances? These problems are not easily solved.

Then what happens to the 4 or 5 percent that are returned annually? How does the retailers know how much to rebate? This Congress is not big enough to get manufacturers to tell the retailer or the consumer what their cost was, and that is what this bill calls for.

How do we implement exemptions? Tandy has several million exempt customers; 5,000 stores pay tax at one rate, 2,000 stores are taxed at another rate; 60 kinds of equipment. What are we going to do?

The CHAIRMAN. Your time is up. Do you want another half a minute?

Mr. ROACH. You have my story. The bill is not needed. It represents bad policy. We urge your opposition.

[The prepared statement follows:]

STATEMENT OF
JOHN V. ROACH
CHAIRMAN OF THE BOARD
TANDY CORPORATION
BEFORE THE SENATE JUDICIARY COMMITTEE
ON
S. 1739
August 4, 1986

My name is John Roach. I am Chairman of the Board, Chief Executive Officer and President of Tandy Corporation. Tandy is a Texas-based company which makes and sells business and consumer electronics products. Tandy has 20 factories nationwide, employs over 27,000 people in the United States and does business with 30 million American households every year. Last year, Tandy's sales passed $3 billion.

The over 7,000 Tandy stores and dealers comprise the nation's largest chain of electronics stores. (A state-by-state breakdown of these stores is attached as Appendix A.) Most of these stores, which go under the name of Radio Shack, Scott, McDuff and VideoConcepts, sell a wide array of audio recorders, audio tape and recording accessories.

I have been part of the Tandy management team for almost twenty years and this is the first time I am testifying before a Congressional committee. Despite a conflict with sales meetings, I wanted to testify. I welcome the honor and the privilege of appearing before this respected committee, and I am here today because I am concerned about S. 1739 and the serious problems it will cause manufacturers like Tandy, and retailers like Radio Shack.

This legislation will force Tandy and every other audio manufacturer to provide confidential pricing information to retailers. It will force retailers like Radio Shack and Scott into a costly confusing transactional mess in an effort to comply with the terms, exceptions and requirements imposed by the tax royalty collection and rebate portion of the bill. The bill, its exemptions, rebates, and proposal for a decoder chip, impose significant increases in our inventory expense, product cost, and administrative burdens and will make our product planning extremely difficult. Moreover, as it is presently drafted, S. 1739 will significantly increase the prices of recorders sold by a vertically integrated company like Tandy.

Tandy is a big company. Tandy will not shut its doors if one of its product lines is rendered unprofitable. But for smaller manufacturers and retailers, this legislation could mean the difference between profit and loss - between survival and going out of business.

We oppose S. 1739. We disagree with the philosophy behind it. This legislation is unnecessary, unfair and unworkable. Its effects on manufacturers, retailers and consumers have not been carefully considered.

THIS LEGISLATION IS UNNECESSARY AND UNFAIR

Before Congress transfers hundreds of millions of dollars from one industry to another and taxes the consumer, it should consider whether a cross-industry subsidy is necessary or fair. I think it is neither.

A subsidy to the recording industry from the consumer electronics industry is absurd. Consider how consumer electronics technology has expanded recording industry opportunities in the past decade.

It is the consumer electronics industry which created the market and demand for prerecorded tape by continually providing new hardware with more features at lower and lower prices. In 1976, prerecorded cassette tape sales were less than four percent of the prerecorded music market. Within the next five years, the boom-box, portable headset tape player and car stereo cassette tape player were introduced. These new products became immediately popular and created an enormous demand for prerecorded music on cassette. By 1984, prerecorded tape sales exceeded record sales. Last year, the recording industry sold $2.4 billion worth of prerecorded tape.

The consumer electronics industry has also created a new market for the recording industry in the form of compact discs. This new software, which digital encoding makes laser readable, has proved to be a tremendous boon to the recording industry. Compact discs were not even sold by the recording industry in 1980. In 1984, the recording industry sold over $100 million worth of compact discs and in 1985, this figure almost quadrupled to $389.5 million.

The consumer electronics industry created the demand for prerecorded cassettes and for compact discs. This legislation attacks the very industry that fueled the recording industry's boom over the last three years. The recording industry, while reaping in all the profits from new consumer electronics technologies (like the compact disc and stereo television) is grabbing for a bonus subsidy off the backs of the industry and consumers which have contributed to its sales growth. This is grossly unfair.

A royalty tax is also unnecessary. Other than stuff the coffers of the big companies and organized groups which can afford the lengthy administrative proceeding to get a share of the royalty tax proceeds, this subsidy will do little to contribute to the creativity it seeks to protect. The few recording artists lucky enough to get a share of the proceeds will face higher costs for their recording equipment. The real struggling artists, which duplicate their own tapes using dual-cassette recorders and send them out to every radio station and record company, will face the biggest burden, as the cost of their recorders skyrockets.

I suggest that the recording industry look to the marketplace rather than to the Congress for its profits. If the recording industry views certain consumer electronics products as a threat it should work in the marketplace around those products

- rather than trying to distort the marketplace through governmental intervention. Let me give you an example.

The recording industry has chosen not to make high quality prerecorded tapes commercially available. Tapers who want high quality music on audiotape must buy a record and copy it. If S. 1739 passes, the recording industry would get a double royalty - both the record and the recording equipment would include a royalty fee. But instead of seeking a tax on the recorders, the recording industry could instead respond to the marketplace by using higher quality audio tape and slower dubbing speeds when making prerecorded cassettes. Although the quality of prerecorded tapes has recently improved slightly, the recording industry would cut down home taping if consumers could purchase the high quality product they want to buy - rather than having to go through the time, trouble and expense of making a high-quality recording themselves.

Until the recording industry looks to the marketplace and fails; until it proves it is losing money; and until it can claim that it is hurt more than helped by consumer electronics technology, then we think this legislation is premature and unnecessary.

THIS LEGISLATION WILL HURT HARDWARE RETAILERS

Selling audio equipment is a tough cut-throat business. Retail casualties are frequent.* Inventory costs are high. Advertising is a large and necessary expense. Customer satisfaction, sales training and warranty service are critical but essential costs of doing business.

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*Major audio hardware retail chains which have recently filed for protection from creditors include: Pacific Stereo (86 stores); Schaak (64 stores) and Tech HiFi (41 stores). In addition, hundreds of non-chain stores have recently closed their doors.

Within the past year audio equipment retailing has even gotten more perilous as large regional retailers have expanded into each other's markets. One year ago today Tandy took the risk of purchasing McDuffs, a 61 store chain and recently purchased the 195 store VideoConcepts chain. These stores will compete with Radio Shack stores in their markets as well as with other existing and expanding retailers.

Given this extremely competitive retail market, industry observers expect a major shakeout within a few years. Many of the major retail chains will survive; several will not. Many small mom-and-pop retailers will unlikely be able to withstand this fierce competition.

Make no mistake, we are not here to complain about competition. We relish it. Nor do we think many smaller retailers would ask Congress to do anything to stifle this competition or interfere with the free marketplace. In fact, I appear today to make sure that the competitive marketplace is protected. I know I speak on behalf of all hardware retailers when I ask you to consider how this legislation will interfere with marketplace purchasing decisions, prices to retailers and to consumers, and inventory burdens for all retailers.

Most importantly, we ask you to consider how the so-called exemptions will work when retailers like Radio Shack sell to non-profit groups or small businesses who are theoretically exempt under the Act.

A. The Act Will Disrupt Retailers' Buying, Pricing and Administrative Decisions

If the Act passes as drafted, we would not only face confused consumers, we would be confused ourselves. As a retailer, should we buy any more recorders for sale - or would we be better off going into the used recorder business to avoid paying or passing on these onerous royalties? Should we order rack systems, recorders with microphones, dictating devices, telephone answering equipment, and audio or computer cassette recorders? How about the thousands of recorders used to tape both music and speaking? Will they be exempt from the royalty tax? We don't know.

Let's see how the royalty tax would work with just three Tandy products which are in Radio Shack's newest catalog.

The Realistic CTR-70 retails for $49.95. It is "capable of reproducing" radio or records. It can tape off of a radio or a record thanks to the auxiliary input jack common to most audio recorders. The Copyright Royalty Tribunal is not likely to exempt this device from a royalty as it clearly is "suitable for making audio recordings by individuals for private use." So anyone who buys this will have to pay a 5% royalty tax. Personally, I don't think this device hurts the recording industry. Maybe some kids can figure out how to hook it up to their record players or radios and make a tape - but mostly these recorders tape lectures, letters, home music and kids having fun.

How about the Realistic Modulaire 850 - a $179.95-boom box? Kids like it because they can get up to two hours of continuous taped music. It has a continuous playback feature which automatically allows listening to two tapes in sequence. What I don't under stand is will the 25% royalty tax fall on just the recording mechanism, or on the entire box device including radio, microphone and speakers?

Or how about the $2000 rack system which is featured on the back page of our new catalog. The dual-cassette recorder is just one part of a TV-HiFi-VCR-radio-compact disc player rack system - plus speakers. Does the 25% royalty tax get put on the whole system, the box or the recording mechanism?

We don't know the answers to hundreds of questions about this bill. S. 1739 raises more questions than it answers. Every piece of hardware is unique so that an enormous question remains as to how specific legislation would apply to it. Radio Shack lists over 60 different types of audio recorders in its catalog.

Most recorders have auxiliary input jacks which if hooked up properly can record off of radios and record players, and therefore fall under the bill. We can't imagine that even the recording industry would suggest that most types of recorders should be subject to a tax - but that is how the bill could be interpreted.

As retailers, we do not take kindly to the government getting involved in the intimate details of our business and disrupting our buying, pricing and administrative decisions. Given the precarious profitability of several retailers, a mistake in ordering based on unknown royalty taxes and misjudged consumer demand could be the costly straw that forces them into bankruptcy.

B. The Royalty Tax Will Inevitably Result In Higher Prices

It does not take an economics degree to know that any tax at a higher point in the distribution line will be in part absorbed by the retailer and in part passed on to the consumer. Further, any price increase born by the manufacturer or importer at the manufacturer's level will have a mark-up. The consumer electronics industry mark-up (or gross margin) has been reported to be about 30%. If a manufacturer must pay an additional 25% for a product it will charge the distributor the additional 25% plus 30% of the 25% to recover its additional costs. The distributor will likewise charge the retailer an additional 20% over this amount and the retailer will charge the consumer an additional increase over the price charged by the retailer. The royalty the consumer eventually pays will be much more than 25%.

C. The Act's Exemption For Recorders With Decoder Chips Will Create A Dual Inventory

The Act creates an exemption from the royalty for recorders which include a decoder chip designed to block copying of encoded software. If manufacturers use this exemption, retailers will face major problems dealing with the problem and expense of a dual inventory.

Retailers of audio hardware will face a Hobson's choice. Either they carry both types of recorders or they carry only one type. If a retailer carries both types, the retailer doubles its inventory cost, purchase expense, carrying cost and floor space used. If it carries only one type, business will be lost to the competitor who carries the other type.

This artificial bifurcation of the audio recorder market will come at great cost to every audio retailer. For retailers who make the wrong product selection or cannot afford the inventory cost, the dual inventory creating provision of the legislation will be especially harmful.

In addition to the enormous inventory costs, the retailer will be forced into the burdensome position of having to explain to the consumers the decoder chip technology, and which recorders work with which software. Sales personnel on the floor will have to explain that a recorder with the decoder chip will record old music and new unencoded music but will not record new encoded music; and that, pre-1987 recorders can record old music and new music, both coded and unencoded. These lengthy and confusing explanations come at the cost of sales time and the customer's interest in our stores and products. We do not need this type of retailing headache.

A decoder chip would also hit hardest the people who can least afford it. The costs of installing a decoder chip would have the largest proportional effect on the cost of lower-end goods.

D. The Royalty Tax Unfairly Penalizes Vertically-Integrated Companies and Smaller Retailers

This royalty tax proposal is absurd for another reason: it imposes a vastly different royalty tax on the same type of product depending on how it is distributed in the United States. Worse, the royalty tax falls much harder on a vertically-integrated company like Tandy than it does on foreign - owned importers. Why is this?

S. 1739 requires that the 5% and 25% royalties be assessed on the "price charged for the first domestic sale" of the audio recorder. The bill defines the "first domestic sale" as the first U.S. sale to an unrelated party. This produces absurdly different results depending on how a company is structured and how it purchases and distributes its products. The royalty tax charged will change depending on whether the percentage is based on the manufacturer, retailer or consumer cost.

If S. 1739 becomes law and a tax is imposed, a company which is not vertically integrated pays the least tax. The "first domestic sale" of the recorder, as defined in the legislation, will likely be the company's F.O.B. U.S. purchase of the recorder. An importing company which does not sell or buy from a related party will pay 5% or 25% of the price it pays for the product.

A company, which imports from its parent company, will pay a tax based on the percentage of the price it charges in its "first domestic sale". As this sale will likely be to a retailer, its tax will be higher.

Tandy and other vertically integrated companies will pay the highest royalty tax as their "first domestic sale" to an unrelated party is to the consumer. A fixed percentage of the consumer price is higher than the same percentage of the retail price or importer's price. Tandy will be put at a competitive disadvantage as it will have to pay a larger royalty.

Because S. 1739 is structured this way, gray market importers will pay a lower royalty tax than authorized distributors, when the authorized distributor is a subsidiary of a foreign company.

Further, if the amount of the tax depends on the price charged anywhere along the distribution line, questions of interpretation arise. For example, is "price" the list price or negotiated price? Does it include discounts, advertising allowances, or key city funds?

Any royalty tax based on price further disadvantages the smaller mom-and-pop retailers who end up paying higher prices and therefore higher royalties. Volume retailers like Tandy's McDuff, which generally get better prices, will obtain an additional competitive advantage over smaller retailers.

E. The Bill's Rebate System for Certain Groups Will Change the Nature of Retailing

The Act purportedly provides for exemptions from the tax for businesses and non-profit organizations. We agree that non-profit organizations should not subsidize aspiring musicians like Michael Jackson or Bruce Springsteen. But S. 1739 provides no guidance on how these exemptions will work. We fear that their implementation will not only be a major bureaucratic headache for retailers, but will create competitive havoc by forcing retailers to obtain the prices manufacturers paid.

The bill provides that the tax will be assessed at the manufacturer's level. Consumers who qualify for a rebate from payment of the tax would have to obtain a rebate from the government, the manufacturer, the distributor or the retailer. Any system created would put a burden on the retailer as it would be the retailer who would have to deal with the confused, irate or bureaucratically worn-out consumer.

Any rebate or royalty-tax avoidance scheme would not be simple to operate. Such a scheme is infinitely more complex than that where a non-profit organization representative flashes an ID card and escapes a local tax. The royalty tax will invariably be incorporated into the price of the machine and retailers would be unable to determine the amount of the rebate.

Would the rebate be based on the manufacturing, retail or consumer price? Would a rebate make allowance for the additional margins added on to the royalty tax at each stage of the distribution chain? What if the product is returned after the rebate is provided?

If the tax is based on the manufacturer's price, a rebate system would require retailers to be told by the manufacturers or importers at the manufacturers level to disclose the percent of the product's cost which included the tax. The retailer would then easily determine the distributor or manufacturer's margin on every recorder. This is totally unacceptable; as this is confidential competitive information. Competitors would also learn of the prices manufacturers are charging retailers.

Consumers entitled to the rebate would also learn of the retailer's or distributor's cost of buying the good. This is unacceptable in the commercial marketplace because consumers have a difficult time understanding the relationship between the retail price and the manufactured price. Overhead, labor, distribution, advertising, interest, warranty service, insurance, and other marketing costs are overlooked by the consumer when being presented with a difference in prices at different points on the retail chain.

But beyond the questions of confidentiality of information is the fundamental issue of whether any rebate or royalty avoidance system would work. From the point of view of this manufacturer and retailer any exemptions are unworkable.

THE LEGISLATION WILL HURT HARDWARE MANUFACTURERS

S. 1739 not only imposes an extremely large but unknown royalty tax on hardware manufacturers, but it would create an intimidating array of expensive paperwork and lengthy administrative proceedings. Armies of accountants will be needed to calculate the percentage of payments, rebates and exemptions for each recording product and for each customer.

Tandy has several million business and non-profit organization customers. We have 7,117 stores and these stores sell over 60 types of audio recorders. As several million customers will be entitled to any one of a thousand types of rebates depending on the product, selling price, and the store, we will have to hire scores of personnel to deal with these administrative burdens. The sheer paperwork will overwhelm us. These costs should be compared to the bill's supposed benefits: the theoretical incentive of creating new music which would otherwise not be created.

This tax and its related costs are so substantial that the bill can only have a serious effect on future technological developments. It is unclear whether the royalty tax will be charged only on the recording mechanism, the entire system or something in-between. Consumer electronics has been moving towards technically integrated systems and any royalty tax which provides an incentive or disincentive for an integrated system would be an artificial interference into a naturally-evolving consumer-oriented marketplace. While today audio and video systems are integrated - in the future we expect audio, video, computer and telephone systems to merge. We can only guess how this tax would affect the cost - if not the sales of any specific product.

In addition to the tax, with its enormous economic burdens, there is the unquestionably large administrative expense every manufacturer will have to endure. As every manufacturer markets a broad array of unique products, the appropriateness of every recorder for the tax will have to be decided by the administrative machinery and eventually by the courts. Even assuming that the numerous ambiguities in the legislation can be resolved by the courts, the remaining paperwork burden will remain.

S. 1739 is not needed. It is bad policy and is an example of unnecessary government interference in the free market system. We urge you to oppose this legislation. The problems it creates for retailers and manufacturers are overwhelming.

APPENDIX A

TANDY CORPORATION

BREAKDOWN OF OPEN RETAIL STORES BY STATE
AS OF 07/29/86

STATE	TOTALS	RS STORES	RS FRAN / DEALER	SCOTT MCDUFF	VIDEO C
AK	20	0	20	0	0
AL	118	67	47	0	4
AR	79	26	53	0	0
AZ	111	72	32	0	7
CA	715	580	89	8	38
CO	135	80	45	0	10
CT	87	83	4	0	0
DC	13	13	0	0	0
DE	25	21	4	0	0
FL	366	276	55	19	16
GA	194	112	76	0	6
HI	16	13	3	0	0
IA	77	42	35	0	0
ID	49	17	32	0	0
IL	297	218	67	0	12
IN	170	113	54	0	3
KS	90	42	46	0	2
KY	114	56	58	0	0
LA	139	81	56	0	2
MA	149	127	22	0	0
MD	119	98	13	0	8
ME	50	21	29	0	0
MI	220	161	59	0	0
MN	114	60	51	0	3
MO	150	86	58	0	6
MS	88	37	48	1	2
MT	31	8	23	0	0
NC	184	134	49	0	1
ND	20	9	11	0	0
NE	52	27	25	0	0
NH	40	19	21	0	0
NJ	163	133	20	0	10
NM	56	32	23	0	1
NV	36	24	11	0	1
NY	387	334	52	0	1
OH	304	242	59	0	3
OK	132	64	63	0	5
OR	110	61	47	0	2
PA	323	262	55	0	6
PR	13	13	0	0	0
RI	24	23	1	0	0
SC	96	53	39	0	4
SD	22	12	10	0	0
TN	156	86	53	14	3
TX	596	383	169	19	25
UT	59	36	21	0	2
VA	181	137	39	0	5
VT	19	9	10	0	0
WA	173	116	50	0	7
WI	152	87	65	0	0
WV	54	27	27	0	0
WY	29	9	20	0	0
TOTALS	7.117	4,842	2,019	61	195

7,117 TOTAL OPEN RETAIL STORES INCLUDED ABOVE

Tandy Corporation
Executive Offices 1900 One Tandy Center Post Office Box 17180 Fort Worth, Texas 76102 Telephone (817)390-3700

John V. Roach
President
Chief Executive Officer
Chairman of the Board
390-3214

1986 AUG 22 AM 7: 57

August 16, 1986

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
226 Dirksen Senate Office Bldg.
Washington, D.C. 20510

Dear Senator Thurmond:

I want to thank you again for having invited me to appear, on behalf of Tandy Corporation and the consumer electronics industry, at the important hearings that your Committee held on August 4 concerning the Home Recording Act, S. 1739. I hope my testimony will help persuade your Committee that this legislation does not deserve its support.

In the course of my answer to one of your questions, Senator DeConcini expressed his frank skepticism about my answer, and I promised this letter for the record, explaining how Radio Shack's business practice could be as I described it.

You had asked me to comment on the Administration's testimony opposing S. 1739 but advocating study of a mandated "decoder chip" system. In part of my reply, I suggested that a mandatory decoder chip system would discriminate against lower priced recorders, because the costs involved would be a higher percentage of these recorders' prices. I said that, according to the administration, the additional manufacturing cost of the decoder chip system would be between $1 and $5, so we should assume a $3 manufacturing cost. I said that once this cost were "loaded" (i.e., marked up) through the distribution system, it would be significantly more, increasing the cost of an inexpensive recorder by up to a third.

Senator Deconcini said he found my response to be incredible. He said that he understood why products are marked up through distribution channels, but that he could not believe Radio Shack or other retailers could or would apply this markup to the manufacturing cost of the decoder chip system. I replied that Radio Shack and other retailers must apply their markups to all of their costs.

I think the nub of my misunderstanding with Senator Deconcini is as follows: If the only costs of the decoder ship system to Tandy and Radio Shack were the $3 increase in manufacturing cost (later assumed to be $2.50 in our colloquy), I could understand and accept Senator DeConcini's point. Any distribution markup above this level, although applied through standard practices, would leave the retailer vulnerable to competition from others, who could cut back their own price increases until the new price reflects only their actual increases in costs.

However, I also made the point (though I didn't explicitly tie it in with this issue) that the increase in manufacturing cost is not the only cost increase that decoder chips (or, for that matter, royalty taxes) would cause. There are many other costs which, I am afraid, would more than require the retail markups that I predicted. First and foremost is the decline in demand for new recorders of all types, since the 138.2 million recorders presently owned by consumers would have an important feature that new ones would lack.* Of equal significance would be customer confusion, and the floor time spent by our sales personnel explaining why new recorders are more expensive yet lack a feature, the types of material these recorders can and can't record, and the information consumers should seek from record retailers. And product and warranty returns, already a major cost, would increase in frequency and complexity. Each of these problems involves training and time of people at every level of the distribution system, so is appropriately figured into the distribution markup.

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* The increased costs associated with this decline in demand would include decreased economies of sale and inventory write-downs. These inventory liquidations, due to inability to foresee demand, could temporarily depress price levels, as retailers absorb their losses, but the long-term result would be fewer recorders on the market, at higher price levels.

I know Senator DeConcini agrees with my basic point that retail markups are necessary because product distribution and sales are necessary services, for which significant costs are incurred. (The recent wave of retailer bankruptcies, to which I referred in my testimony, illustrates this. If retailing were pure profit, these would never occur.) I hope that I have now clarified the relationship between the distribution and retailing costs associated with any decoder chip system, and the retail markups applied to the manufacturing costs of such a system. Accordingly, I trust that Senator DeConcini will accept that my answer was well supported and given in good faith.

I strongly believe that the $1 - $5 figure given as the "cost" of decoder chips is only the tip of the iceberg. The hidden costs which I discuss above are important, additional reasons to oppose S. 1739, and any other legislation involving decoder chips. I was pleased to appear before your Committee, Mr. Chairman. Please let me know how I can be of assistance in the future.

Sincerely,

John V. Roach

John V. Roach

cc: Hon. Dennis DeConcini

enclosure

NORMAL MARK-UPS FOR MERCHANDISE FROM POINT OF MANUFACTURE TO RETAIL CUSTOMER

GROSS MARGIN EFFECTS OF INCREASED MATERIAL COSTS

Basic Material Cost	$10.00	
+ Labor & Overhead	2.00	
SG&A	.50	
	12.50	
Factory Profit - 8% G.M.	1.08	
Factory Selling Price	$13.58	
Importer/Sales Co.		]
Selling Exp., Advertising		]
Credit & SG&A	$ 4.27*	] 30% Distributor Margins
Distributor Profit - 8% G.M.	1.55	]
Distributor Selling Price	$19.40	]
Retail		]
Rent, Advertising,		]
Salaries & SG&A	$ 6.31	]
Retail Profit - 8% G.M.	2.24	] 30.59% Retail G.M.
Retail Selling Price	$27.95	]

*Includes duty and freight for imports

ADDITIONAL

Add $2.50 in material cost of decoder Chip today

Basic Material Cost	$10.00	
+$2.50 Decoder Material	2.50	
+ Labor & Overhead	2.20	(Inc. due to added components)
+SG&A	.50	
	15.20	
Factory Profit - 8% G.M.	1.50	
Factory Selling Price	$16.69	
Importer/Sales Co.		]
Selling Exp., Advertising,		]
Whse., Salaries & SG&A	$ 5.24	] Maintaining 30% G.M.
Distributor Profit - 8% G.M.	1.91	]
Distributor Selling Price	$23.84	]
Retail		
Rent, Advertising,		]
Salaries & SG&A	$ 7.40	]
Retail Profit - 8% G.M.	2.71	] 29.8% G.M.
Retail Selling Price	$33.95	]

$\frac{\$33.95}{\$27.95}$ = 21.5% Increase in Selling Price

The CHAIRMAN. Mr. Eugster, would you care to make a 5-minute opening statement?

STATEMENT OF JACK W. EUGSTER

Mr. EUGSTER. Yes, I would. Thank you.

The CHAIRMAN. Now, you understand your entire statements can go in the record if you have a fuller statement. Just give us the thrust of your position.

Mr. EUGSTER. My name is Jack W. Eugster. I am chairman and chief executive officer of the Musicland Group, Inc., the Nation's largest specialty retailer of sound recordings, headquartered in Minneapolis, MN.

I am also a director and past president of the National Association of Recording Merchandisers [NARM], and am here representing both the position of my company and NARM.

I am pleased to be here today to have the opportunity to testify in support of S. 1739, the Home Audio Recording Act, which would place a royalty on audio recording devices, with proceeds from such royalty to be distributed among owners of sound recordings and music copyrights, lyricists, composers, vocalists, and musicians.

At present time, our company owns 515 stores located in 46 States. We are retailers of all kinds of sound recordings, including compact discs, long-playing records and cassettes. We also sell portable audio hardware products in most of our stores, and prerecorded video products in all of our stores.

NARM has 196 members who operate over 9,000 stores and departments throughout the United States.

It seems evident from the various studies which have been made that the ready availability of audio recording devices has significantly cut potential sales of records and tapes. Private studies I have seen have shown that one-fourth of all music copying is done from albums and tapes borrowed from friends, and 17 percent of copying is from the radio. This is not right, and it is not right to make copies for friends either.

As you have been advised by representatives of major sound recording companies, most recordings do not return a profit. Thus, support of creative efforts in the music field, with its concomitant development of new artists, suffers if sufficient funds are not available for creative development.

The development of new artists in critical to the success of the record business, including record retailers. Much investment is needed to expose new music and new artists to the public. This is not a very predictable process, and thus a reasonable return for everyone involved is needed to keep new music coming.

Widespread home taping clearly reduces in a substantial way the availability of funds for creative work. The bill would accomplish the dual objective of compensating those who have suffered from the effects of home taping and making available additional funds for creative efforts.

Development of an individual as a creative artist is a difficult and expensive process that only occasionally yields substantial returns to the artist and/or promoter. Such individuals, therefore, are in great need of aid which can be provided by this legislation.

Home taping would not be prohibited by the legislation. In fact, it would be specifically permitted. In return, the manufacturers and importers of sound recording devices would be required to compensate copyright holders and the artist for revenues lost as a consequence of such taping.

We do not believe that the royalties proposed in S. 1739 would have a significant adverse impact on the sales of audio hardware. The normal royalty to be paid as set forth would be 5 percent of the value of the first sale in the United States.

Thus, a unit costing at wholesale $250 would have a royalty of $12.50. Even with markups, the added cost to the consumer would not be great, and certainly not the 30-percent numbers we heard.

Devices capable of more significant copying—that is, dual audio recording devices—would have a 25-percent royalty on the first domestic sale. Devices with more than a dual capacity would be considered infringing devices and illegal.

The approach taken by S. 1739 is similar to that adopted or being considered by a number of foreign countries which face similar home taping problems. In our opinion, the United States should be no different.

Intellectual property owners should be fairly compensated for their creative efforts. S. 1739, if enacted, would help to remedy the imbalance created by home taping. For that reason, both the Musicland Group, Inc., and NARM support S. 1739, as reported by the Subcommittee on Patents, Trademarks and Copyrights.

I will be pleased to answer any questions.

The CHAIRMAN. Thank you very much.

Mr. Jarman, would you care to make a 5-minute statement?

STATEMENT OF EDWARD JARMAN

Mr. JARMAN. Yes, Senator. Thank you very much.

I thank you for inviting me to testify on the Home Audio Recording Act. My name is Ed Jarman. I am a record retailer. I own four Peppermint Record Stores in Greenville, SC, one of them near the campus of Clemson University.

My history includes management positions with London Records in the midseventies, Polygram distribution from 1977 through 1980. Polygram is a European conglomerate; they own RSO, Mercury, Polydor, Casablanca, Philips, and Deutsche Grammophon.

As a company vice president working in New York, I was involved in the corporate policy and decisionmaking process. I am here to testify against S. 1739, legislation which would tax audio recording machines. I very much am opposed to the previous bill, which also taxed blank audio tapes and is still pending in the House.

I do not like the new bill any better, and I am surprised that legislation which only taxes audio machines is seen as some kind of compromise. Taxing the machines people use to listen to the music they have bought from the record companies makes little sense and is unfair.

I guess it is not enough that my customers buy the record industry's records. Should they also have to pay to listen to them?

Having been both a record company executive and a record retailer, I believe I can offer a unique perspective on why the current version of S. 1739 is a bad idea and should not become law.

As a former record industry executive, I can tell you that home taping is not the threat the RIAA claims it is. I worked in the industry during the slump of the early 1980's when all of the home taping was supposedly taking place.

If they were not blaming home taping then, the industry's tailspin during this time period could be directly attributed to bad judgment, overspending and overexpansion. It was only after the Sony Betamax case when we saw the movie studios demand to be paid a royalty on video recorders and video tape that the idea of asking for a royalty on audio machines and blank tape came up.

All of a sudden, home taping was the culprit. Well, I did not believe it then and I do not believe it now.

The record companies say that they are losing significant sales because of home taping, but I disagree. As a record retailer, I can tell you that I gain more sales as a result of home taping than I lose.

First of all, most of my customers do not tape at all; they do not have the time to invest in it—people who want to buy cassettes, even though the quality is inferior to records and discs.

Other customers, mostly my record buyers, do tape, but mostly to preserve their records, which scratch and wear out. My store near the Clemson campus does an excellent business. The college students are good customers and I have talked to many of them.

I am not concerned that they tape some of their purchases because if some of these customers could not tape, they would never have bought the record in the first place. If they did not tape, their friends may not have gotten interested in the music and they never would have become my new customers.

All of these horror stories about kids taping records fail to look beyond the actual taping to what is really happening. More music is being bought by these kids as a result.

In summation, I do not see any reason to go after these college students that you are so worried about. Even if you wanted to do something about them, why tax all of my other customers.

There is a provision in this bill which so threatens me that I also have to mention it. I understand this bill provides for an exemption for equipment containing encoder/decoder technology which would prevent the taping of prerecorded music which has a signal built into it.

Practically speaking, this technology would obligate me to carry two kinds of prerecorded music for every record, tape, and compact disc without the signal. I would also carry another record, tape, and disc with the signal. Carrying six versions of every title would be a disaster for me.

If I wanted to continue carrying all the titles I presently carry, I would be forced to significantly increase my floor space to accommodate increased inventories. I will need a larger store and, of course, rents will go up.

Carrying this dual inventory also doubles the risk of my business decisions. Maybe the large record chains represented by NARM can handle this, but a small seller like myself will be hard-pressed.

My immediate reaction would be to cut down on the number of titles I carry. Clearly, the less well-known artist and the struggling artist this bill purports to help will suffer because I will have to make room for all the versions of the music of more popular artists.

Perhaps most importantly, the whole idea of encoded records, cassettes, and discs will confuse and anger the customer. I will lose much of the goodwill I have worked to create over the years.

I am fearful that the changes that are being considered by this committee today can have additional effects that I cannot predict. But even on the basis of what I have pointed out today, I think it could be big trouble if this legislation becomes law.

It is hard enough to keep my customers in the store without taxing the very machines my customers use to enjoy their music. I urge you not to do it. It makes no sense; it is not necessary. Please oppose S. 1739.

[The prepared statement follows:]

Testimony of Ed Jarman
before the
Senate Judiciary Committee
on S. 1739

August 4, 1986

Thank you for inviting me to testify on the Home Audio Recording Act. My name is Ed Jarman and I am a record retailer. I own four Peppermint Record stores in South Carolina, one near the campus of Clemson University. My work history includes management positions with London Records in the mid-70s and Polygram distribution from '77-'80. Polygram, a European conglomerate, owns RSO, Mercury, Polydor, Casablanca, Philips, and Deutsche Grammophon. As company Vice President working in New York, I was involved in the corporate policy, and decision making process.

I am here to testify against S. 1739, legislation which would tax audio recording machines. I very much opposed the previous bill which also taxed blank audio tapes and is still pending in the House of Representatives. I don't like this new bill any better and I am surprised that legislation which "only" taxes audio machines is seen as some kind of compromise. Taxing the machines people use to listen to the music they bought from the record companies makes little sense and is unfair. I guess it's not enough that my customers buy the record industry's records; should they also have to pay to listen to them?

Having been both a record company executive and a record retailer, I believe I can offer a unique perspective why the current version of S. 1739 is a bad idea and should not become law. As a former record industry executive I can tell you that home taping is not the threat the RIAA claims it is. I worked in the industry during the slump of the early '80's when all this home taping was supposedly taking place. We weren't blaming home taping then. Our major concern was the commercial counterfeiting of records and tapes that cost Polygram an estimated $100 million on records by Donna Summer, the Bee Gees, and the soundtracks Grease and Saturday Night Fever.

More generally, the industry's tailspin during this time period can be directly attributed to bad judgment, overspending, and overexpansion. The RSO record label's Grease and Saturday Night Fever generated hundreds of millions of dollars for the company, yet 18 months after the biggest selling record in history RSO was out of business. Now comes the recession and finally tremendous competition from video games and arcades taking away 100's of millions of leisure dollars from the record companies. The results were disastrous. Every company, CBS, WEA, Capitol and Polygram ordered personnel cutbacks as much as 50% and started closing branch offices. It was only after the Sony Betamax case and we saw the movie studios demand to be paid a royalty on video recorders and video tape that the idea of asking for a royalty on audio machines and blank tape came up. All of a sudden home taping was the culprit. Well, I didn't believe it then and I don't believe it now.

The record companies say that they are losing significant sales because of home taping, but I disagree. As a record retailer I can tell you that although I may lose a few sales from home taping, I bet I gain almost as many as I lose. First of all, most of my customers don't tape at all. They don't have the time to invest to do it. People who want portability buy cassettes (even though they are of inferior quality to records and discs). Other customers, mostly my record buyers, do tape, but mostly to preserve their records, which scratch and wear out.

Still other customers, a minority, are real audiophiles and they may tape a lot of their own records or tapes. These people, who are into music enough to tape it, are often my best customers. These people perform a function much like the radio. They spread music around so other people hear it. For example, some of my customers make their own customized tapes of favorite selections and then they play these "party tapes" for friends. However they share their love of music with friends, these audiophiles help me sell more music because their friends end up coming to my store to buy records of the groups they learn about.

My store near the Clemson campus does a good business. The college students are great customers. I've talked to them. I'm not concerned that they tape some of their purchases, because if some of these customers couldn't tape, they would never have bought the record in the first place. If they didn't tape, their friends may not have gotten interested in music and they would never have become my new customers. All these "horror" stories about kids taping records fail to look beyond the actual taping to what's really happening: more music is being bought by these kids as a result.

In sum, I don't see any reason to go after these college students you're so worried about. And even if you wanted to do something about them, why attack all my other customers?

One excuse I hear for this legislation is that it will help the struggling artist. When I was an executive at Polygram, the record companies didn't really care about the struggling artists. What everyone in the record industry cares about is sales volume and the bottom line. And that's as it should be. The record companies want to make money. If pouring money into the established artists will make money, that's what they'll do. And it's what they are doing. It's also the bottom line that's pushing this legislation because if this bill passes it means lots more money for the record companies. But more money for them doesn't at all mean more money for struggling artists, or cheaper prices for consumers, or even better profits for record sellers like myself.

Until today I had never met a record retailer who supported this legislation. But now I see that the National Association of Record Merchandisers is testifying today for the bill. I think they do a disservice to the entire music industry and to their customers by being here in favor of the tax. I understand how NARM, which represents the big chain record stores, might not want to oppose the record companies, but I can't believe they have reasons to support this legislation.

Perhaps they believe that more money to the record companies would mean more money to the record sellers, but I know better. Even when the record companies do well it doesn't mean more money for us. In the last two years there have been at least two increases in the wholesale price I have to pay for my stock of records, cassettes, and discs while the retail selling price has remained constant. This profit taking by the record companies has forced many small record retailers out of business. When I read in the trade press how great the record companies are doing, I find these price increases hard to justify. According to the July 19 Billboard Magazine, CBS Records' second quarter profits rose 55 percent from last year's second quarter. For the first six months of this year CBS Records' profits were $81.4 million compared with $43.8 million for the first half of 1985. The only time CBS Records has had better profits was in 1984. (Where was home taping then?) What this tells me is that the industry is going gangbusters over the last three years, and still my costs go higher and higher. Why should I think further enriching the record companies will help me? With them already doing so well, I'm frankly surprised to see RIAA still pushing this tax and Congress still taking them seriously.

Not only am I not going to benefit from this legislation, I'm likely to be seriously hurt. I question whether the record companies have the best interests of the industry at heart. In pushing this bill, the record companies are attacking the retailers; the customers; and the manufacturers of record players, cassette machines and compact disc technology: all the people who have helped create this industry. This tax could kill a good thing. If you make machines more difficult to buy, you'll be taking customers out of my store.

I am here today to stand up for my customers who are outraged when they hear about this legislation. I consider my family a representative U.S. household. I personally own two auto cassette players, one Walkman, one home cassette player and my two children have portable cassette players (jam boxes). We use these machines for playback only and we have never duplicated a record or tape. The record industry wants millions of people taxed to get to the few who tape prerecorded music; that's extremely unreasonable.

There is also a provision in this bill which so directly threatens me that I have to mention it. I understand this bill also provides for an exemption for equipment containing special encoder/decoder technology which would prevent the taping of prerecorded music which has a signal built into it. Practically speaking, this technology will oblige me to carry two kinds of prerecorded music. For every record, tape, and compact disc without the signal, I would have to carry another record, tape, and compact disc with the signal. Carrying six versions of every title would be a disaster for me.

If I want to continue carrying all the titles I presently carry, I will be forced to significantly increase my floor space to accommodate the increased inventory. I'll need a larger store to do this, and of course, my rent will go up. Carrying this dual inventory also doubles the risk of my business decisions. Maybe the large record chains represented by NARM could handle this, but a small record seller like myself will be hard pressed. My immediate reaction would be to cut down on the number of titles I carry. Clearly, the less well-known artists, the struggling artists this bill purports to help, will suffer because I will have to make room for all the versions of the music of more popular artists. Perhaps most importantly, the whole idea of encoded records, cassettes, and discs will confuse and anger my customers. I'll lose much of the good will I've worked to create over the years.

The whole music industry is doing very well right now, but I know how fragile this success can be. The record companies understand that the music customer can be priced out of the record store. An example would be the plight of the country music buyer. In the past, country records were priced less than pop records. When list prices were raised to the same levels as other music categories, sales plummeted. The country customer was not willing to pay $9-10 for a record or cassette; the exception being country cross-over artists like Kenny Rogers, Willie Nelson, Dolly Parton and Alabama. Knowing how fragile the business is, I would think the record companies would be careful about tampering with the existing market.

I am fearful that the changes being considered by this Committee today can have additional effects I can't predict. But even on the basis of what I've pointed out today, I think we could be in big trouble if this legislation ever becomes law. It is hard enough to keep my customers in the store without taxing the very machines my customers use to enjoy their music. I urge you, don't do it. It makes no sense and it isn't necessary. Please oppose S. 1739.

In conclusion should the record labels require another several hundred million dollars in profits, let them use legislation and laws that are in place. The prerecorded music counterfeiter is thriving in North and South Carolina. They have counterfeit RCA, CBS - in fact, all major label - cassettes for sale in hundreds of flea markets and convenience stores throughout our area. This is against the law, and its taking away revenue from every record company and Peppermint Records. If you have to give the record companies something, please enforce the laws that exist, but don't attack my customers and my business; that will help no one.

The CHAIRMAN. Thank you very much.

I would like to ask all of you one question; we will just start with Mr. Roach, Mr. Eugster, and then Mr. Jarman. What is your feeling concerning the administration's position?

Mr. ROACH. Well, I think the question that the administration brought up is one for decoders, and certainly it gets rid of the royalty tax, which is absolutely impossible as far as it has been proposed.

But the decoder itself has a lot of adverse possibilities. If you take, for instance, this tape recorder that we sell for $27.95—and most people do not understand the distribution channels and the costs, but those raw materials are probably on the order of $10.

If you add from $1 to $5—say you add $3 cost at that $10 level. That means you have added approximately $9 at retail to the price of a low-end unit, and $9 on $27, I believe, comes up to the 30 percent that I had mentioned earlier.

Senator DECONCINI. Mr. Chairman, I am not that good a mathematician. How would a 5-percent royalty on a $27 item amount to $9? Would you explain that?

Mr. ROACH. Well, Senator, we are talking about the decoder portion, and the decoder has been variously described as $1 to $5 for the chips and/or circuitry associated with it.

Of course, that has got to be loaded at the factory level, the gross margin maintained on it as it is imported, if it goes through——

Senator DECONCINI. Let us just work that out. You say $1 to $5. Let us say it is $2.50. You add that on to that cost of that machine there, so that is $27, and you add $2.50 to it, and then you add 5 percent on top of that?

Mr. ROACH. Whoa, whoa. You are adding at the wrong place. This $2.50—a decorder chip is added at the manufacturer's level and it will be marked up at each level in the chain.

Senator DECONCINI. Why do you have to markup at that level when you are marking up the machine? You have already got your markup on the machine.

Mr. ROACH. The retail business—you have got to maintain your gross margins and mark up on cost, and the decoder chip would be a cost——

Senator DECONCINI. You do not mark up on every single item that is in that machine, do you?

Mr. ROACH. We certainly do.

Senator DECONCINI. You mark up at the total——

Mr. ROACH. We mark up at the manufacturing plant, we mark up at the wholesale level or distributor level, and you mark up at the retail level.

Senator DECONCINI. So you are going to take a dollar chip and make a profit each time you resell that?

Mr. ROACH. We have to. We are going to make a profit on every other chip we have got in that unit. Why are we going to treat this one chip separate?

Senator DECONCINI. Because you make an unconvincing argument to an opponent to the bill that the Tandy Corp. would go out and make money on a little bitty chip when you are already making money on your operation.

I know your operation well in Arizona and you do a great job. I cannot imagine that you are trying to tell us here that you have got to make a profit on a $1 chip.

Mr. ROACH. Well, it is not a function of just Tandy Corp. It is a function of electronic distribution, and all costs will be marked up at every link, every level in the channel.

So I do not care whether you are a U.S. company, whether you are a Sony, whether you are an importer like Sound Design; I do not care who you are. The manufacturing cost of the machine is going up by the decoder chip, and when the manufacturing cost goes up, that is carried throughout the system.

Senator DECONCINI. Mr. Chairman, thank you. I will not interrupt you anymore and I do not have any other questions. I just would say that that is the most unconvincing argument I have heard today. The most unconvincing argument because it does not make sense.

I know your people's operation in Arizona. They are tenants of our shopping centers and they do a great job. I know some of your managers out there. They tell me that they do not mark up every item.

That just does not make any sense. I happen to be against it for other reasons, but not because you guys are going to have to make another profit on each little item.

Mr. ROACH. Senator, I would like to provide an example to the committee at a later date showing them how this markup would work.

The CHAIRMAN. I think you better clarify that because you are under fire a little bit now from your own Senator.

What is your feeling about the administration's position?

Mr. EUGSTER. Yes. My feeling is that in the long run the idea of some technical solution to the problem, such as the chip, is a good idea. I want to state strongly that in the short run, we need to have this bill to protect the copyright holders now.

With regard to some of the math that has been used here, I understand the cost of the decoder chip may be as low as $1. If, in fact, you were to be as generous to say that the full retail price might be $10, if you use a $20 item, perhaps it gets to $30.

If you use a $50 item, which I would still consider to be low, it is a 20-percent markup. If the item is $300 at retail, it is a 3-percent markup. So I think the math can be a little misleading.

Nonetheless, my position is that the decoding in the long run is a good idea. This bill is needed today because the long run is quite a ways away.

The CHAIRMAN. Mr. Jarman, what is your position toward the administration position?

Mr. JARMAN. I am in agreement with the administration. I am a friend of the record industry. If the record industry is healthy, I am healthy. If they are not doing well, I am not doing well.

I earn my total income from my business. I have no outside interest. My record stores provide me with my style of living.

The record industry would enjoy a short-term windfall if this legislation went through, and I think that would make everbody happy—the NARM people and the chain record stores. But, in fact, the long term of this bill could be crippling to the industry.

It would force me into carrying inventories, and record retailers like myself that cannot afford to carry these multiple inventories—it would force us into that position. In fact, we compete with Musicland in our town and we compete with record bars in our town.

It would put us in an uncompetitive position that the majors such as the Musicland Group—they receive favorable terms from the record companies. They receive favorable discounts from the record companies and favorable advertising to put these inventories in place.

So the short term would, in fact, be very beneficial, but every time the record industry loses outlets, they reduce their position to sell records, and that is exactly what this will do. With multiple inventories, this will put businesses such as mine out of business.

Senator SIMON. If the Chairman would yield on that——

The CHAIRMAN. I would be very pleased to yield.

Senator SIMON. So if you had a choice of the administration proposal or this bill, which would you prefer?

Mr. JARMAN. I would say that the administration should, in fact, let the marketplace determine what needs to be done.

Senator SIMON. You favor the status quo, obviously.

Mr. JARMAN. Oh, certainly, certainly.

Senator SIMON. But many of us feel that the status quo is, frankly, not adequate; that people are not getting compensation for their creative work.

Mr. JARMAN. The record companies—these are very smart people. They will react to a problem. This reaction of CBS developing a chip—that is a part of their reaction to it. This is not something that is new; for years, it has been going on.

Yet, my sales of prerecorded tape—I have been in business 6 years this January. Cassette sales at one time represented about 20 percent of my business. Today, prerecorded cassette sales represent 65 percent of my business.

The customer that they are saying is stealing their artistry is, in fact, the customer that is supporting them. The manufacturer of a home taping machine or a portable machine—and that is really what broke our industry. That is what really put us into this boom era, the portability of a tape; that you can take this little tape in your boat, and you can put it in your car and you can put it in your travel home.

That is what really got our industry from a large industry to a multibillion-dollar business. So, now, the recording companies, in looking for additional revenues, what they are doing is they are trying to stifle this.

Again, I am a friend of the record business. I am supported by the record business, but on this issue I disagree with them.

Senator SIMON. I think you, Mr. Chairman.

The CHAIRMAN. Thank you. Senator Simon, I have to get to the floor for this defense bill. Could you take over the hearing now?

Senator SIMON. I will temporarily. Unfortunately, I am going to have to leave in about 15 minutes.

The CHAIRMAN. Now, I observe that Ms. Dicksie Cribb, the mother of assistant attorney general Kenneth Cribb, is here. I believe you are with Ms. Lucille Ward, so when she comes up, if you want to come up and join her and make a statement, we would be glad to have you do so.

I am going to ask Senator Simon, then, if he will take over.

Senator SIMON [presiding]. If I may ask, do you pronounce your name Roach or Roach?

Mr. ROACH. Roach.

Senator SIMON. Which do you favor; the administration proposal or this bill?

Mr. ROACH. Well, certainly, the royalty tax is absolutely unworkable, but the question of whether anything is required, one, and, two, if a decoder as described is really justified because, unfortunately, I do feel it does put a substantial additional cost into equipment to the consumer, and that may be out of proportion with the real benefit to be obtained from it.

The whole decoder concept is a very new concept, and I think before anybody should accept what has been proposed, there needs to be far more engineering studies of the feasibility.

In general, the free airways have prevailed and it is the software provider who has the responsibility to protect their software.

Mr. SIMON. You mentioned that the bill as it now is framed puts you at a disadvantage vis-a-vis foreign competitors and other competitors.

Can the bill be changed in such a way that we still encourage creative artists and yet do not put companies like yours at a disadvantage?

Mr. ROACH. Well, certainly, the various levels at which the tax is levied at the present time makes it a very unlevel playing field and it is totally unworkable. Can the thing be fixed?

You know, this has been debated for a number of years and really no workable solution has been developed until the present time, so I do not know.

Senator SIMON. I cannot speak for the chief sponsor, but my guess is that we would be interested in any practical suggestion that could be made along that line.

I am going to turn the chair over to my senior colleague at this point.

Senator MATHIAS [presiding]. Do you have any further questions?

Senator. SIMON. I do not.

Senator MATHIAS. The one question I would have for the panel is really a very general question. The problem with which this committee is faced is that we have on the books of the United States some laws which attempt to protect the intellectual property rights of people who hold copyrights.

Now, we sees those rights being eaten away under the impact of modern technology. Many of us believe there is a problem here, and I think the administration's testimony this morning indicated that the administration sees a problem as well.

What do we do? You are the real experts in this field. You are workers in the vineyard and you are practical fellows who know what the problem is. What do we do about it?

Mr. ROACH. Well, you know, you really have a question as to there possibly is some problem, but there are an awful lot of legitimate uses, very appropriate uses of tape recorders and recording equipment.

Technology, as you indicate, is moving very quickly. There has been some discussion of DAT, digital audio tape, here this morning. Who knows whether that will be an important new technology, whether it will mix audio and video?

I think the history has shown us, though, that industry and software owners and royalty owners have typically had the responsibility to protect their own proprietary interests, and this is what has happened in the satellite area; it is what has happened in the computer software area.

I think it is a little but unusual that this particular segment of technology is being treated differently or being looked at differently than some of those other areas have been.

Senator MATHIAS. Well, let me stipulate that I think that as a result of modern technology, there are a number of appropriate uses for duplicating equipment and other mechanisms to make copies.

I certainly do not rule that out. But it is not solely your particular corner of this problem that is troubling us.

Xerox machines are essentially the same problem with the printed page. It is not one corner that is involved; it is a broad problem.

Perhaps, as you say, it is not up to you to suggest the answers. However, if you do not like the answers that we find, then I ask you for alternatives.

We have got a problem and we are reaching out for the best way we know to solve the problem.

Mr. ROACH. Well, unfortunately, technology probably is working against a solution more than it is working toward a solution because the natural integration of circuitry that is going on, what part of any product sold today is actually a tape recorder and what part is for other purposes—are these in the circuitry? Is there common circuitry between the things that are done?

We show on the back of this new catalog a $2,000 video—audio system that has VCR's included in the same system with tape decks and possibly a compact disc, and what have you. Entertainment technology is very broad; it is very pervasive and it is moving very fast.

It is really driving this industry and driving the need for prerecorded materials, in my opinion, much more than it is inhibiting that industry.

Senator MATHIAS. Let me just ask you this question: Is the equipment that you just referred to in your catalog patented?

Mr. ROACH. There may be patented circuits in——

Senator MATHIAS. Or are patents pending?

Mr. ROACH. Well, there may be patents pending; there may be patented circuitry in various of these products. There may be patented circuitry in some of these tape recorders that we talked about earlier.

But, certainly, I think it has been well established over time that I can loan my car or my tape recorder to somebody and that does not violate the use of the patent on that particular device.

Senator MATHIAS. Well, I was not really reaching for that point. I just was wondering whether your company had applied for patents. That would indicate to me that you have some respect for the concept of intellectual property; that you like that protection.

Mr. **Roach**. Well, Tandy Corp. particularly has a real respect for intellectual property in the area, say, of computer software where we are a major software developer and use copyrights there, and what have you.

The other side of the coin—we fully recognize that it is our responsibility to protect our copyrighted material; that we cannot depend on the U.S. Government to do it for us.

Mr. **Jarman**. Senator, I would like to say that the record companies are seeking additional revenues, additional profits. The artists are requesting or are in need of additional royalties.

A major problem in North and South Carolina is cassette counterfeiting. Years ago when I was a part of this when we were attempting to get legislation to protect the artists and protect ourselves against the counterfeiters, this was the P legislation in the early 1970's when there was a proliferation of just tens of millions of eight-track tapes, and a great deal of them coming out of the Carolinas.

I believe that particular manufacturer was taken care of and stopped, but what is happening today is in convenience stores and in flee markets in North and South Carolina, you can buy an "Alabama's Greatest Hits" that is a counterfeit tape. It is not a tape that has been made on a Memorex tape and duplicated and it has typed across the front of it "Alabama's Greatest Hits."

It is a tape that is duplicated. Everything leads the customer to believe that this is an RCA tape. The same is true of major hits by CBS and Warner Brothers. They are openly sold in my home State and in our neighboring State of North Carolina.

The revenues that are being lost through these sales are astronomical to the record companies. There are astronomical royalties being lost to the artist. And to me as a retailer, we have people that bring in these counterfeit items and they will say to us, we bought this.

We do not require a receipt to exchange a defective item, and they will say we bought this and it is defective. Will you give us a new one? Upon—it is not really close examination—on examination, it is easy to determine for us, being record people, that this is, in fact, a counterfeit.

It goes on day in and day out and there are millions of dollars involved. There is legislation to stop it. The record companies could gear up and put their energies in that area.

The Government could, in fact, support the record industry and they will gain the revenues they are talking about with this legislation plus more if they could stop the counterfeiting.

Mr. **Eugster**. Senator, may I add something?

Senator **Mathias**. Let me just ask whether you reported this to the Department of Justice?

Mr. **Jarman**. Oh, certainly, certainly. In fact, in our area one of the largest flea markets in the Southeast is in Anderson, SC. I own a store in Anderson, SC.

The FBI has come to the Anderson flea market and actually taken inventories, and it made the business section of the newspaper. They have done it more than one time. Yet, at this flea market when I was last there, which was about 4 weeks ago, there was a person there selling counterfeit tapes.

Senator MATHIAS. After the FBI had been in?

Mr. JARMAN. Yes; that is correct.

Senator MATHIAS. Well, the committee will make some inquiry about that. I think it is important that everyone in the industry who has such knowledge should cooperate with the Department of Justice and should provide information. As you say, it is against the law and we all have some duty with respect to seeing that the law is enforced.

Mr. Eugster.

Mr. EUGSTER. Senator, I do not quite understand why counterfeiting is being brought into this session. However, I would, for an informational basis——

Senator MATHIAS. As an alternative source of revenues. [Laughter.]

Mr. EUGSTER. Maybe I do understand.

For information purposes, I might like to say that the RIAA maintains a very aggressive anticounterfeiting effort, along with the Government, I understand, and our company actually contributes to that effort financially, as well as providing information when we see counterfeit tapes. We try to provide that information.

You asked what should we do with regard to this problem. It seems to me, and maybe this is a bit philosophical, but our country is built on trying to protect certain people's rights—really, everybody's rights.

Sometimes we have to face solutions that seem to be some kind of compromise. This bill does a pretty good job of that. It protects the rights of intellectual property owners, while at the same time not taking away the rights of equipment manufacturers.

There is a rebalancing that obviously goes on, but this bill seems to be in the tradition of protecting as many people's rights as possible.

Mr. ROACH. Senator, if I could comment just one more time, you were asking about possible solutions. Certainly, there is an absolute solution. In fact, you know, if people pay a royalty and they feel like they have an unlimited right to copy and use the thing, this could work just as much to the detriment of the industry as anything.

But one of the things I think the prerecorded tape industry could do is to try to mark on their cassettes, put audio tracks on their cassettes, much stiffer warnings, much stiffer suggestions that these things not be copied. I believe there are a lot of people that are morally influenced by things such as this.

Senator MATHIAS. I think that is a thoughful suggestion. The question of the educated consumer is one that is appropriate in many areas of our economy and our society. Is there a place for your company to educate consumers?

Mr. ROACH. Certainly, as I mentioned earlier, we spend a great deal of time educating consumers, people that walk into our retail stores. However this issue is ultimately resolved, our retail sales force will bear a big part of the burden of educating the consumer.

Senator MATHIAS. But educating them about the rights of copyright owners?

Mr. ROACH. Well, again, we do not know what we have got to educate them about, but it that what is ultimately passed by this Congress, obviously that is what we will be doing?

Senator MATHIAS. The law currently establishes the right of the copyright owner, and I do not believe that is in any doubt. How it is to be enforced is the question we are wrestling with, and I think an organization such as yours could be a very great help in educating consumers on that question.

Mr. ROACH. We have been very cooperative with both the industry and the Government in endeavors in the past, and certainly we are always open.

Senator MATHIAS. A few boldface boxes in that catalog might help.

Mr. ROACH. They are worth a lot of money, but we would certainly be glad to cooperate. I think you will find, if you read the text of that catalog, it is written in a very professional way that in no way supports illegitimate or inappropriate uses of tape.

Senator MATHIAS. Thank you very much, gentlemen. We appreciate very much your presence here today.

The next panel, panel No. 3, consists of: Mark Silbergeld, of the Consumers Union; Mr. Oral Miller, national representative of the American Council of the Blind; Ms. Lucille Ward, immediate past president of the National Federation of Music Clubs; Ms. Jane King, deputy director of the National Consumers League; Mr. Frank Yudkin, vice president of the Consumers Association of Kentucky.

Since this is a very large panel, we are going to ask each of you of confine your oral statements to about 4 minutes, and we will have the light system. Then that will leave us time for some questions.

Who would like to begin?

STATEMENT OF A PANEL CONSISTING OF MARK SILBERGELD, DIRECTOR, WASHINGTON OFFICE, CONSUMERS UNION; FRANK YUDKIN, VICE PRESIDENT, CONSUMERS ASSOCIATION OF KENTUCKY; ORAL O. MILLER, NATIONAL REPRESENTATIVE, AMERICAN COUNCIL OF THE BLIND; LUCILLE WARD, IMMEDIATE PAST PRESIDENT, NATIONAL FEDERATION OF MUSIC CLUBS, ACCOMPANIED BY DICKSIE CRIBB; AND JANE M. KING, DEPUTY DIRECTOR, NATIONAL CONSUMERS LEAGUE

Mr. SILBERGELD. I would be pleased to go first, Senator Mathias. Thank you very much.

Let me state at the outset in response to the colloquy that took place between Senator DeConcini and previous witnesses, that we do not in any way defend copying to avoid purchase.

We believe that the act of copying to avoid purchase is not one which should be protected. The question is how does that fit into all home taping activities, and is it serious enough that anything should be done about it?

We think that the answer is, at least on the basis of what we have seen so far and the bills that have been put forward to cure the asserted problem—the answer is nothing.

S. 1739 and the administration bill would both place substantial burden on consumers who purchase home taping hardware, and the administration bill explicity, and S. 1739 permissively, could perhaps place a burden on consumers of the software in retail stores through the use of chip encoding as well.

The royalty that is proposed as a solution for the asserted problem, we believe, falls upon infringing and noninfringing uses of the hardware, on those who copy to avoid purchase and those who copy for other reasons, which we believe at least some of the studies to show is a great majority of all home copying activity.

We believe that the record is especially void on the key question, which is what does home copying do to creativity. It is still not clear to me after the many hearings before your subcommittee, Mr. Chairman, and the hearings here today who is not creating as a result of home copying.

One agrees that is may be impossible to document the specifics of that, but the assertion in the absence of evidence seems to be somebody, without any specifics, and we do not believe that this sustains the proponents' burden in urging changes in a law that is meant primarily to protect creativity, rather than to tax each and every enjoyment that may result from a copyrighted product or creative effort, but to encourage creativity.

The question has arisen with the other witnesses, and I may as well anticipate it, what about the administration's proposal. What I see is two bills, each of which could result in chip encoding, whether by mandate or by incentives through the law that encourage that, alternatives neither of which are good for consumers, one of which would be tremendous confusion and additional costs on the hardware end and creating a tax on the hardware end, the other quite possibly creating confusion on the software end.

If you thought that consumers were confused, for instance, when telephone services were unbundled, you are going to see a cameo of that if consumers start seeing six formats of software in the record store.

I do not think the consumers welcome that. We have heard from at least one retailer who says he certainly does not welcome that. I think the end effect of that may be to discourage creativity, as the multiplicity of formats that have to be carried and judged as to the mix of inventory that should be carried drives the smaller creative artists right off the shelf.

I would be happy to answer questions when you get to them, Mr. Chairman. Thank you.

[The prepared statement follows:]

Testimony of

MARK SILBERGELD, DIRECTOR
WASHINGTON OFFICE
CONSUMERS UNION

Mr. Chairman and Members of this distinguished Committee, Consumers Union* appreciates the opportunity to testify before you in opposition to S.1739, the Home Audio Recording Act. We believe that any changes in the Copyright Act must be justified by a convincing showing that such changes are necessary to promote the Act's purposes. This is especially true where a direct result of a proposed change would be to substantially increase prices for a consumer product and where an indirect result may be very substantial confusion in the retailing of related products. We do not believe that the proponents of S.1739 have carried that burden. Therefore, we urge the Committee not to act favorably on this bill.

S.1739 would place on all consumers who use home recording equipment the burden of compensating for asserted losses suffered by supposed copyright infringement resulting from home copying. True, Section 2(a) purports to "confirm" that a person who makes a home copy for non-commercial use is exempt from infringement liability. But, unless it is newly created by enactment of this bill, there is no legal infringement from non-commercial home copying on which to base liability or an "exemption" therefrom . Home copying for personal use is lawful.

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*Consumers Union is a nonprofit membership organization chartered in 1936 under the laws of the State of New York to provide information, education and counsel about consumer goods and services and the management of family income. Consumers Union's income is derived solely from the sale of Consumer Reports, its other publications and films. Expenses of occasional public service efforts may be met, in part, by nonrestrictive, noncommercial grants and fees. In addition to reports on Consumers Union's own product testing, Consumer Reports, with approximately 3.5 million circulation, regularly carries articles on health, product safety, marketplace economics and regulatory actions which affect consumer welfare. Consumers Union's publications carry no advertising and receive no commercial support.

Nonetheless the effect of the bill is to change the law by making home copying an infringement, exempting the "infringing" party from direct liability and creating a system whereby compensation for the newly created infringement is collected indirectly from the manufacturer who makes new home recording devices. This scheme would tax those who infringe and those who do not, those who copy to avoid purchase and those who do not, alike, by imposing a royalty on recording devices.

This new scheme would diverge from the purpose of the Copyright Act. The Act currently provides copyright holders with protection of their creations in order to encourage ongoing creativity from which society as a whole will benefit. The copyright holder's profit derives from that basic societal interest. The Act does not and should not guarantee to the holder of any copyright payment for each and every copy of the copyrighted work that another may enjoy or for each and every enjoyment that may result. But that is what S.1739 would accomplish.

Therefore, any claim to a legislated right to increased profits from the sale of copyrighted works, where there is no loss from "infringement", as that term currently is legally defined, should bear the burden of showing both that the asserted loss is real and that it results in reduced creativity. We do not believe that the hearings before the Subcommittee have substantiated either claim.

I must hasten to add that we in no way defend home copying for the sole purpose of avoiding purchase. It is not a defensible practice. And there is no reasonable doubt that this practice occurs with some frequency. But it does not follow that the practice requires a legislative remedy, and certainly not a remedy such as that proposed in S.1739, which falls on all purchasers of new home recording equipment whether or not they copy to avoid purchase. Further, there are other, very legitimate reasons for home copying which should not result in additional compensation to the copyright holder which would fall within the purview of S.1739.

It has not been convincingly shown that the totality of home copying practices result in a net loss to copyright holders or in reduced creativity. Studies of home copying behavior performed for the recording industry and the electronics industry claim, not surprisingly, startlingly differing results. The recording industry studies claim that a high percentage of all copying activity simply reproduces a copyrighted program "as is" to avoid purchase. The electronics industry studies claim to demonstrate that the net effect of home recording may actually increase the sale of copyrighted materials. The latter studies report that many copyrighted recordings are purchased because the buyers wish to use them to arrange their own tape programs from multiple recording sources or to create a more portable copy from a disc. In other words, the machine creates the pre-recorded program sale. These studies also suggest that "as is" pass-ons from a purchaser of a commercial recording to a non-purchaser may stimulate the non-purchaser's subsequent purchase of other copyrighted material by the same recording artists.

We are not prepared to judge the relative competence and merit of these behavioral surveys. It should suffice that the recording industry, which should have the burden of establishing its conclusions of fact over competing, contrary conclusions, has to date failed to do so.

We must add, also, that certain technical qualities of copyrighted commercial recordings create legitimate consumer incentives for copying such materials.

First, the commercial availability of many items tends to terminate long before the copyright expires, creating a legitimate consumer incentive to copy instead of purchase simply because the item is no longer available for purchase. It is, after all, a purpose of the Copyright Act to increase the availability of creative works to the public. Second, when there are no pressing defects, a vinyl disc is typically superior to the commercial cassette version of the same program, creating a legitimate consumer incentive to purchase the vinyl disc and create a home cassette copy for portable listening. Third, vinyl discs are subject to serious damage and wear, creating a legitimate consumer incentive to make archive copies of purchased items or to treat the original as the archive copy and play the home-taped copy in order to safeguard the investment in the disc. Fourth, compact discs are the most preferred medium for home listening, while cassettes --preferrably re-recorded with compression-- are the preferred medium for car listening, creating a valid consumer incentive for copying CD programs to cassette.

Thus, much of home copying is consistent with the purposes of the Copyright Act and the copyright holder should receive no more additional compensation for these copies than their own ingenuity and the market can create.

The recording industry might argue that such copying uses are not fair, and that consumers who want to enjoy a program in more than one medium must purchase it in each medium that they desire. But this would only confirm the industry's view that the Copyright Act serves to tax enjoyment, rather than to promote creativity.

Previously, the recording industry pointed to lowered profitability as evidence that it was suffering economically from home copying to avoid purchase. But, following a series of financially unrewarding years preceding 1984, the recording industry as a whole enjoyed record high revenues and profits in 1984. And this trend has continued in 1985 and 1986. The dip in profits preceding 1984 occurred during a very serious recession, when virtually every industry suffered. And it occurred during the height of popularity of video games, a strongly competing form of home entertainment. There is absolutely no evidence of decreased incentives to create new audio home entertainment programs.

The industry seems to have fully recovered. Further, the advent of the compact disc presents a windfall to the recording industry, as music lovers replace existing recordings already in their library with new performances of the same works, and even with the same performances in the new format, in order to enjoy the new technology. Indeed, if anything, this technology-driven development may at the same time increase profits and somewhat decrease the incentive for creativity as there is a shift to replacement of identical materials in a new format. But the point is that the industry cannot point to a pattern of lowered profitability and blame home copying for it.

Section 119(c)((1)(C), as revised under the bill, could be used to create an especially disruptive situation in the retailing of pre-recorded audio entertainment programs. That provision authorizes the Copyright Royalty Tribunal to exempt from royalty fees any device technically unsuitable for making audio recordings by individuals for private use. This creates incentives for the marketing of machines --for which the technology already exists-- with the capability of recording only those pre-recorded programs that lacked a copy-defeating electronic signal. Recording firms would offer encoded programs at a lower price than programs that were susceptible to home recording because they lacked the encoding. Retailers would be under competitive pressure to carry six inventories of the same program : encoded and unencoded vinyl discs, encoded and unencoded cassettes, and encoded and unencoded compact discs. Instead of judging the demand for three formats, retailers would have to judge and stock to meet the demand for six formats of the same program. And the demand would change constantly as the new, decoding-capable home recording equipment gradually replaced much of the old equipment.

Doubling the number of products for which retailers must meet demand undoubtedly will increase the rate at which demand is misjudged and, thus, the unavailability of programs in the format the consumer wishes to buy.

Further, your subcommittee has heard testimony that such an increased inventory requirements will mean a greater allocation of shelf space to popular items at the expense of such creative products as jazz, contemporary classical and children's programs in order that the retailer may minimize lost sales due to out-of-inventory situations. The crowding out of less popular, highly creative materials would reduce the marketability of creative ideas, and thus the incentive for their creation -- a result directly contrary to the purposes of the Copyright Act.

In closing, I hope the Committee will keep in mind that no given level of profit is the purpose of the Copyright Act -- its purpose is to encourage the creation and wide dissemination of new ideas. Even reduced revenues, were they to be demonstrated, would not justify S.1739, but only lost creativity. We believe that the record utterly lacks convincing evidence that home recording reduces creativity.

Senator MATHIAS. Thank you.

STATEMENT OF FRANK YUDKIN

Mr. YUDKIN. I am Frank Yudkin. I am with the Consumers Association of Kentucky. I am here as an attorney and as a member of our association, but not only for Kentucky, but the millions of consumers across the country.

I want to register our opposition to 1739. The Louisville Times, in an editorial against the bill on July 25 of this year, said:

> Perhaps the most grievous part of the tax proposal is its basic unfairness. The tax would punish the innocent along with the guilty because everyone would have to pay even if they used tapes and tape decks to record live concerts, speeches, or the grade school Christmas pageant.

We have two big military bases in Kentucky, Fort Campbell and Fort Knox. I know that there are many families of these servicemen who use tape recorders to send verbal messages to the servicemen around the world.

College students—when I went to college, I also recorded my lectures, and we have colleges in Kentucky and those students use it, too. That would be the unfairness of it.

In reviewing the letters from the consumers that were sent to the various Senators, you see people writing that, you know, I use my equipment to record the National Public Radio. Why should that be prohibited? I use it for tape recording Christmas music or teaching.

People from Florida write in saying I record to preserve my original copy for future use. People from Oregon write in and say I buy records and tapes so I can play them in my pickup truck and in my Walkman. People from Pennsylvania write in and say on simple moral grounds, I vehemently disagree with the concept. Why should I have to pay for something that I might do with the tape?

Consumers from Massachusetts wrote in and said the record companies have a lot of nerve; they want to tax us on recording equipment. It is just unfair.

Any possible exemption for tape recordings unsuitable for making audio recordings for private use are left entirely to the discretion of the Copyright Tribunal. I think this is an exceedingly broad and unjustified delegation of power to them.

I think what you have to have is something that is fair to the consumer, something that the consumer would say, you know, this is fair. We are dealing with consumers looking forward to an age of increasing fairness in tax reform. I think you should have the same thing here.

Last night, I sat down and tried to write my daughter, who is 10 years old, a letter at camp explaining what I was doing here in Washington and trying to look at both sides. To explain to a 10-year-old that she is going to be taxed for trying to copy something off the radio or, you know, that she could use my old machine at home to copy something off the radio, but if she went out and bought a new machine when she gets to be 16 it would ot copy it, just did not make a lot of sense to me.

I know she is a 10-year-old and maybe does not vote, but I think she is going to, you know, get to that age. I think consumers want something that is fair. They want to be able to do it for their own use, but it should be that we should have these piracy mills out there pumping them out—you know, thousands of copies, hundreds of copies, or tens of copies. Once they start doing that, I think the law should go after them.

But I think home use is a different matter. I think it should be allowed for home use.

Thank you, Mr. Chairman.

[The prepared statement follows:]

Statement of Frank Yudkin
Before The Senate Judiciary Committee
August 4, 1986

Mr. Chairman, Members of the Judiciary Committee.

My name is Frank Yudkin. I am an attorney from Louisville, Kentucky, and appear before you today as a representative of the Consumers Association of Kentucky, of which I serve as vice president. The Consumers Association of Kentucky was formed in 1965 and is the only statewide non-governmental consumer organization in Kentucky.

On behalf of the members of the Consumers Association of Kentucky and millions of our fellow consumers around the country, I want to register our opposition to S.1739, the Home Audio Recording Act.

Stated in simplest terms, this proposal will hurt consumers. In fact, the Louisville Times, in its editorial against S.1739 (July 25, 1986), states "Perhaps the most grievous part of the tax proposal is its basic unfairness. The tax would punish the innocent along with the guilty because everyone would have to pay even if they used tapes and tape decks to record live concerts, speeches or the grade school Christmas pageant." Why should consumers who use their recorders for these purposes be forced to pay a royalty tax to the recording industry?

And there are so many other consumer uses for tape recorders other than taping pre-recorded music.

Kentucky is fortunate two large military bases, Fort Campbell and Fort Knox, and thus we know that members of our armed forces stationed around the world and their families use tape recorders for verbal correspondence. Why should they be required to pay a royalty tax to the recording industry?

College students take tape recorders into classes to record lectures. I know, I did myself. Why should they be required to pay a royalty tax to the recording industry?

Let me quote from a few of the letters received from consumers by the Audio Recording Rights Coalition.

Mr. Gillett of Salem, Oregon writes: "I use my equipment for live recording and recording radio broadcasts on National Public Radio. I do not duplicate copyrights records." Why should he be required to pay a royalty tax to the recording industry?

A letter from Mr. D. Strang from Kent, Ohio: "Most of my taping is of Christian music or teachings. I don't want to subsidize anti-Christian music."

Ms. Mansione from Tampa, Florida: "I record my albums to preserve the original copy's value in the future. Everyone keeps trying to get a bigger chunk of my hard-earned dollar...."

Mr. Baker from Adams, Oregon says: "I like to buy records and tape them so I can play in my pick-up and in my Walkman." Why should these people be required to pay a royalty tax to the recording industry?

Another consumer writes: "On simple moral grounds, I vehemently disagree with the concept that I should be made to pay for something that I might do with tape recording equipment." This is from Mr. Gibson of Narberth, PA.

From Mr. Osburne of Princeton, NJ: "Royalty taxes on cassette decks or integrated circuit spoiler systems to prevent home taping are attempts by the recording industry to force consumers to pick up the tab for their poor business practices."

Mr. Berube of East Hampton, Mass. says: "The record companies have a lot of nerve. Now they want to tax us on recording equipment? The principal is down right unfair."

From Mr. Venneberg - Topeka, KS: "This is unfair to all the people who use cassette recorders, etc. for their own benefit and enjoyment. Congress has enough and more important problems to worry about instead of passing laws so companies like the record industry can make another easy buck by not doing a darn thing!"

And Robin Blier - Annandale on Hudson, NY: "Who would this bill help? A few wealthy record and tape companies. Who would it hurt? The general public."

I realize that S.1739 has so-called exemptions for non-infringing use. But any possible exemptions for tape recorders unsuitable for making audio recordings for private use are left entirely to the discretion of the Copyright Royalty Tribunal. This is an exceedingly broad and unjustified delegation of power to a federal agency without the resources and proven track record to justify such power. In fact, S.1739 gives no assurances that such exemptions would be provided at all. Indeed, the Copyright Royalty Tribunal, under S.1739, could deny any exemption to the new royalty tax. And, it is highly doubtful that any exemption mechanism can be devised that would be both fair and facile to administer. The one thing we can be sure of is that S.1739 will help expand the federal bureacracy. Although the bill does provide the funds for the CRT to administer the new royalty tax program, it surely will require additional CRT employees and office space which only add to the troubles of this controversial agency. Why should the consumer pay to finance unneeded additions to the federal bureacracy?

The Home Audio Recording Act, in short, seems neither necessary nor desirable. It will be costly to consumers who tape pre-recorded music for preservation or portability. It will prove grossly unfair to consumers who do not tape prerecorded music at all but who will have to pay a royalty tax to the owners of music copyrights.

Consumers look forward to an age of increased fairness and tax reform, not to an age of catering to a special interest and additional tax burden.

I strongly urge you to recognize and reject this S.1739 for the anti-consumer measure it is.

Thank you.

Senator MATHIAS. Thank you very much.
Mr. Miller.

STATEMENT OF ORAL O. MILLER

Mr. MILLER. Thank you very much, Mr. Chairman, and distinguished members of the committee. I am Oral Miller, the National Representative of the American Council of the Blind, which is the largest membership organization of blind and visually impaired people in the United States.

We sincerely appreciate this opportunity to testify today about the Home Audio Recording Act because we are vitally interested in all legislation and programs that impact on our members.

The Home Audio Recording Act is such a piece of legislation, and I am here today to discuss with you some of our concerns. We basically see three main problems with this legislation.

First, the royalty fee disproportionately affects blind purchasers. For the past 25 years, the American Council of the Blind has worked to improve the lives of blind people through legislation, legal advocacy, public education, membership training, and other services.

Our members live in all parts of the country and come from all walks of life. Some own their own businesses; some are employed in a great variety of occupations. However, many are unemployed or severely underemployed, and many of them subsist on supplemental security income, Social Security disability insurance, or other government programs.

Whatever their status may be, though, one thing is certain, and that is a majority of the blind people in this country own and use audio recording devices and they need to continue to be able to purchase such devices.

Many educators and blind scholars believe that the audio recorder is the greatest educational aid for the blind since the invention of Braille approximately 150 years ago. The audio recorder's usefulness and popularity are based on the fact that it is fast and simple to operate. It is small and portable, such as this little fellow in my hand right here, the size of a package of cigarettes.

Also, the tapes can be stored very easily and the information can be retrieved quickly. But above all else, it is relatively affordable. An additional tax would impose a severe hardship on those people, frankly, who are least able to afford the equipment at current prices.

Blind and visually impaired people rely on recording equipment for a variety of purposes, such as listening to talking books, for use in business settings, to record lectures, to take notes, to listen to college and other educational materials, to listen to prerecorded music, and to record broadcasts such as those of the Radio Reading Services for the Blind on a delayed basis.

In short, the purposes for which recording equipment can be used are endless.

Now, as for the amount of the royalty fee or the tax, we think it is naive to believe that the 5 percent or whatever it may be as the tax will be the only additional cost that is passed on to the blind consumer.

Unfortunately, we are all too familiar with that multiplier effect that was referred to earlier by which each step in the distribution process adds on the specific additional charge plus an additional markup, which is based in some way on that additional tax or royalty.

Our second concern is this: The blind are not exempt under this bill and, frankly, there is not a workable way for exempting them. Unless the American Council of the Blind and other nonprofit organizations wish to become purchasing agents for their members, the exemptions that are listed in the bill simply are of no use to blind consumers.

As a private, nonprofit organization, the American Council of the Blind would qualify under section (c)(D)(i) as being able to purchase these devices minus the royalty tax. But the council would not be able or be willing to buy such equipment for sale to its members.

Such purchase or resale would necessitate additional staffing, warehousing facilities, inventory control, greatly increased financing, and all sorts of other business resources.

If the committee is considering exempting blind people from the royalty fee, the thought is certainly appreciated. Yet, it is completely unworkable. Would blind people have to obtain a license in order to identify themselves as eligible for exemption?

Would the tax be eliminated by the retailer upon sale to the blind consumer, or would a rebate system of some sort be used? Whatever the case, it is clear that blind people would be put in a very difficult position of having to prove their eligibility for the exemption.

My third and final point is that this act would punish those who use audio recording devices for any purposes. There have been anecdotes and some studies saying that home taping has a harmful effect on record sales, but there have also been other studies, plus a lot of other significant evidence, showing that tape recorders are tremendously beneficial to recording artists.

In light of the fact that the penalties and implications of any legislation to tax recorders and to make their use difficult or more complicated would have serious consequences for our members and all blind people throughout the United States, we ask you to take our firsthand evidence and our deep concern into consideration.

We ask you not to tamper with the conditions under which audio recorders are sold. It is our judgment that this bill is not necessary and would, in fact, have harmful effects on blind people, as well as sighted consumers.

In conclusion, the Amercian Council of the Blind again urges the committee to ignore the approach of S. 1739 when considering issues relating to home recording. Again, we thank you for this opportunity to testify and, naturally, we will be glad to answer any questions.

[The prepared statement of Mr. Miller follows:]

STATEMENT OF THE AMERICAN COUNCIL OF THE BLIND

BY ORAL O. MILLER, NATIONAL REPRESENTATIVE

Mr. Chairman: The American Council of the Blind appreciates this opportunity to testify concerning the Home Audio Recording Act. The American Council of the Blind is the nation's largest membership organization of blind and visually impaired people. As such, we are vitally concerned with the programs and legislation which impact on our thousands of members. The Home Audio Recording Act is such a bill, and I am here today to speak on behalf of our membership.

We see several problems with the Home Audio Recording Act, summarized as follows:

1. The Home Audio Recording Act taxes consumers who purchase home audio recording devices. The "royalty fee", or tax, will have a disproportionate impact on the thousands of blind and visually impaired people who rely on such devices for a variety of purposes.
2. The Home Audio Recording Act contains no exemptions for blind or visually impaired customers. However, even if one were to be added, it would create an administrative nightmare and would be an unworkable solution.
3. The "royalty fee" punishes consumers, such as the blind, who purchase and use home audio recording devices.

I. THE ROYALTY FEE DISPROPORTIONATELY AFFECTS BLIND PURCHASERS

For the past twenty-five years, the American Council of the Blind has worked to improve the lives of this nation's blind and visually impaired citizens, through legislation, legal advocacy, and public education. Our members come from all walks of life and reside in all parts of the country. Some of the Council's members own businesses; others are employed in a variety of occupations. Unfortunately, however, many of our members are severely underemployed or unemployed, subsisting on Supplemental Security Income, Social Security Disability Insurance, and other government programs. Whatever the status, one thing is certain;

a majority of the blind in this country own audio recording devices and need to continue to purchase them.

Many educators and blind scholars believe that the audio recorder is the greatest educational aid since the invention of braille 150 years ago. Its usefulness and popularity is based on the fact that it is fast and simple to operate; it is small and portable; the tapes can be stored easily; tape recorded information can be retrieved quickly; and, above all else, it is relatively affordable. An additional royalty tax would impose a severe hardship on those individuals who are barely able to afford the equipment at current prices.

Blind and visually impaired people rely on recording equipment to listen to talking books; for use in business settings; to record lectures; to take notes; to listen to prerecorded music; and to record broadcasts, such as those of the radio reading services for the blind. The purposes for which these machines are used are endless. As stated above, an additional tax would disproportionately burden blind and visually impaired consumers who simply must purchase this equipment. It is naive to believe that the 5% or 10% tax on devices will be the only cost passed on to the blind customer.

II. BLIND PERSONS ARE NOT EXEMPT UNDER THE ACT, NOR IS THERE A WORKABLE WAY OF EXEMPTING THEM

Unless the American Council of the Blind and other non-profit organizations wish to become purchasing agents for their members, the exemptions listed under the Home Audio Recording Act are of no use to blind consumers. As a private, non-profit organization, the Council would qualify under section (c)(D)(i) as able to purchase these devices minus the royalty tax. However, the Council has no intention of purchasing equipment for ultimate sale to its members. Such purchase and resale would necessitate additional staffing, warehouseing facilities, greatly increased financing, and additional business capabilities.

If the Committee is considering exempting blind persons from any royalty fee, the thought is appreciated, yet completely unworkable. It is difficult to imagine a system which would function efficiently and effectively to accomplish this purpose. Would blind people have to obtain "licenses" which would identify them as legally blind or visually impaired? Would the tax be eliminated by the retailer upon purchase, or would a "rebate" system be instituted? Whatever the case, blind people would be put in the difficult position of having to prove eligibility for the exemption.

III. THE ACT PUNISHES THOSE WHO USE AUDIO RECORDING DEVICES FOR ANY PURPOSES

There have been anecdotes and some studies saying that home taping has a harmful effect on record sales. There have been other studies plus significant evidence showing that tape recorders are beneficial to recording artists. In light of the fact that the penalties and implications of any legislation to tax tape recorders and make their use difficult and more complicated would have serious consequences for our group, we ask you to take our firsthand evidence and deep concern into consideration. We ask you not to tamper with the conditions under which tape recorders are now sold. It is our judgement that this bill is not necessary and would have harmful effects on blind and visually impaired as well as sighted consumers.

IV. CONCLUSION

The American Council of the Blind urges the Committee not to take the approach of S.1739 when considering issues relating to home recording.

Thank you for allowing us to share our views with you today.

Senator **Mathias**. Thank you, Mr. Miller.
Ms. Ward.

STATEMENT OF LUCILLE WARD

Ms. **Ward**. Mr. Chairman, I am Lucille Ward, from Greenville, SC, immediate past president of the National Federation of Music Clubs, and I am here to testify on behalf of both the National Federation of Music Clubs and music lovers throughout our great country.

It is an honor for me to be here to express to you our support of S. 1739. May I begin by saying that the National Federation has no interest in this home audio recording bill for any monetary gain.

The cornerstone upon which our 600,000-member organization was founded in 1898 was for the promotion of American music. For 88 years, we have worked with that one goal in mind, that of making America truly beautiful through music, with never a thought of any monetary remuneration.

Ours has been the task of ensuring that our American artists are given opportunities which are their birthright. We take a moment here to thank you distinguished gentlemen for your support in granting a congressional charter to our National Federation of Music Clubs, the third musical organization to be so honored.

We approach this question from a different angle, that of the rights of those who have made possible the copying of these tapes in the first place. We are deeply concerned by the tremendous harm being done to American music by this home taping of prerecorded music.

It is shocking to hear that 75 percent of all blank tapes bought in the United States are used to copy copyrighted music or that the number of new records released in the past 10 years has declined by 43 percent.

The result, fewer choices of music for the public, fewer opportunities for the creative artist, fewer job opportunities, et cetera. The practice of home taping seems relatively harmless, but then millions tape the equivalent of hundreds of millions of albums annually, the economic foundation of our music history is badly damaged, threatening our artists, musicians, publishers, record companies, and thousands who depend on music for their livelihoods.

Not only are we making it an impossibility for our musicians to earn a living, but we are destroying all incentive for their creative talents, thereby forcing them to turn to professions other than music.

What a tragic loss it would have been had home taping forced composers as George Gershwin, Cole Porter, and Victor Herbert to turn to other careers.

It is for preserving and encouraging this God-given talent that our National Federation is working. It is our system of copyright founded in the Constitution that has made America the world leader in music, and which has given the public the variety of music available today.

Yet, it is the other countries that have taken the lead in enacting home audio recording legislation. France recently became the 11th country to establish a reoyalty system to compensate the creators and producers of music. The United Kingdom recently announced its intent to add a royalty on blank tapes. Other nations are moving in the same direction.

For those who argue that individuals should be exempt from liability for infringement by home recording, we agree, but we urge an exemption balanced by an equitable system in exchange to assure fair compensation to copyright owners.

S. 1739 would do this. It would further support young talent because two percent of the amount collected would be given to the National Endowment for the Arts to be used for grants to young musicians.

BMI once used the slogan "the day music died." Have you ever thought seriously what that really means? It is frightening. Can you imagine a world without music? Music is the speech of the angels. It is God's best gift to men, the only art of heaven given to Earth, the only art of Earth we take to heaven.

Who of us does not have a favorite tune or wish that we could play a musical instrument? Who of us has not been inspired by a gospel hymn or the beautiful marches of John Philip Sousa when our soldiers came marching home from battle?

We ask that you support S. 1739, helping us to assure that our musical heritage will be preserved for all generations. This can be possible only if we compensate fully our musicians and producers for their creative talents so that we nor those yet unborn will ever see the day music died.

Help us, the world's largest philanthropic music organization, to save America's music.

[The prepared statement of Mr. Ward follows:]

Statement of Lucille Ward Before the Senate Judiciary Committee on the Home Audio Recording Act, Aug. 1986

Mr. Chairman, and distinguished members of the Senate Judiciary Committee -- I am Lucille Ward, immediate past president of the National Federation of Music Clubs, and I am here today to testify on behalf of both the National Federation of Music Clubs and music lovers throughout our great country. It is an honor for me to be here to express to you our support of S. 1739.

Let me begin by saying that NFMC has no interest in this home audio recording bill for any monetary gain. The cornerstone upon which our 600,000 member organization was founded in 1898 was for the promotion of American music. For 88 years we have worked toward one goal -- that of making America truly beautiful through music.

We here take a moment to thank you distinguished gentlemen for your support in granting a Congressional charter to NFMC -- only the third musical organization to be so honored, and which President Reagan signed into law August 9, 1982.

We are deeply concerned by the tremendous harm being done to American music by the home taping of prerecorded music. It is shocking to hear that 75% of all blank audio tapes bought in the U.S. are used to record copyrighted music and that, since 1978, the number of new albums released has declined by 43%.

The result: fewer choices of music for the public; fewer opportunities for the creative artist; fewer job opportunities -- and on and on.

The practice of home taping may seem harmless, but when millions tape the equivalent of hundreds of millions of albums yearly, the economic foundation of our music industry is badly damaged -- threatening our artists, musicians, publishers, record companies, composers and thousands who depend on music for their livelihoods.

Not only are we making it an impossibility for our musicians to make a living, but we are destroying all incentive for their creative talents, thereby forcing them to turn to professions other than music, so that they may earn a living. It is this young, budding God-given talent in which our NFMC is so interested and which we are working to encourage.

For those who argue that individuals should be exempt from liability infringement for home recording, we agree -- but, we urge that that exemption be balanced by an equitable system in exchange, to assure fair compensation to copyright owners. S. 1739 would do this. S. 1739 would further support young talent because 2% of the amount collected would be given to the National Endowment for the Arts to be used for grants to young musicians.

I particularly want to insure that this legislation does not impose any burdens on the blind and handicapped. We of NFMC are especially interested in this because included in our hundreds of annual scholarships and awards are a number specially designated for the blind and disabled. What a thrill it was when I, as NFMC President was able to send a blind girl from New York to attend the Aspen summer music festival in Colorado -- or again when I was able to give a $1,000 check to a disabled student to continue study in composition at New York University.

Mr. Chairman, as I understand it, this legislation enables organizations of the blind and handicapped to purchase equipment for their members without paying a royalty, under regulations to be established by the Copyright Royalty Tribunal.

We hope that such organizations will take full advantage of this special exemption. If the Congress feels that this approach will not go far enough in responding to the special needs of the blind and handicapped, a more specific exemption can be inserted so that the Tribunal's guidelines would authorize direct purchases by the blind and handicapped without the payment of any royalty.

But let me return to the broader problem. BMI once used in its advertising the slogan, "the day music died." Have you ever thought seriously what that really means? It is frightening. Can you imagine a world without music? "Music is the speech of the angels." It is the only language in which we cannot say one mean or sarcastic thing. Who of us does not have a favorite tune or wished that we could play a musical instrument? Who of us has not been inspired by the beautiful music of John Philips Sousa when our soldiers came marching home from battle? Or who of us has not put a child to sleep with a lullaby?

Music is God's best gift to man. "The only art of heaven given to earth, the only art of earth to heaven." Music is a necessity from the cradle to the grave.

We ask that you, as members of the Judiciary Committee, and as members of Congress, support S. 1739, assuring us that our music heritage will be preserved for our children and those yet unborn. This can be possible only if we compensate fully our musicians and producers for their creative talents, so that our children will never live to see "the day that music died," because of the lack of our support of their creative ability.

Senator Mathias. Thank you very much, Ms. Ward.

Ms. King.

STATEMENT OF JANE M. KING

Ms. King. Yes, Mr. Chairman. I am Jane King. On behalf of the National Consumers League, I want to thank you for inviting us to share our views today on S. 1739, the Home Audio Recording Act.

The National Consumers League has worked for economic and social justice throughout our 87-year history. We support this legislation because we believe it is consistent with our two fundamental goals—assuring economic justice in the marketplace, and fair compensative for workers.

The legislation before you today to provide compensation to creators and producers of music is consistent with these goals and is not, as some have suggested, anticonsumer. Most people regard home taping and the technologies that make it possible as a wonderful opportunity for consumers. They can obtain prerecorded music without paying for it.

After all, would we not like to be able to freely duplicate many products on the market without paying for them? We know, however, that the benefits of such a marketplace are short term and illusory. Simply, put, if we consumers are not willing to pay a fair price for the goods and services we obtain, the producers will justifiably stop producing them and we will all be losers in the end.

The legislation now pending before the full committee is substantially different from the bill that was orginally introduced. Although we supported the original version of S. 1739, we accept certain changes that have now been made and applaud others that have greatly improved the legislation.

Specifically, the proposed royalty on blank tapes has been removed and will now be placed only on equipment capable of direct recording and tape duplicating. In addition, the subcommittee adopted a distribution system for the royalty pool which will assure that substantial portions of the proceeds are used to develop new talent, thereby increasing consumer choices for music purchases. The distribution will be weighted in favor of recordings which are not high on the sales chart but are often new and specialized music.

The manufacturers of recording equipment are benefiting financially from the broad consumption of their products for the express purpose of home taping prerecorded music. We believe that they are profiting substantially from the labors of the musicians and artists, but have failed to recognize their responsibility to compensate them in some way.

In our view, consumers need both the hardware and the software. The equipment would be of little value to the consumers without prerecorded music.

The music industry is declining because of the growth in home taping. We know that there have been 43 percent fewer new releases since 1978, and it is substantiated that jobs have been lost. Consumers again lose out when the variety of prerecorded music available to them is reduced.

Consumers also lose out when home taping results in reduced support for the more specialized forms of music, such as jazz, classical, folk, and gospel. Consumers of music also lose out when the growth of home taping means record companies must raise their prices to those who buy their records because there are fewer sales over which the companies can spread their costs.

Consumers lose out when talented young men and women are discouraged from pursuing careers as musicians, vocalists, or composers.

It is in our interest as consumers to assure the musicians and the artists of adequate compensation for their creations. We also believe that the entire Nation benefits when Congress acts to uphold the principles of copyright. Our Constitution specifically recognizes the need for our Nation's copyright system to promote the arts. This system serves as a model to other countries around the world. We must not let the United States fall any further behind in upholding basic copyright principles.

Ironically, American music is one of the few industries that has a positive balance of trade. Continued erosion of the base which rewards American artists and musicians for the fruits of their labors will surely subvert this balance.

American consumers have a finely developed sense of fairness. Asking those who copy prerecorded music to pay for the privilege of doing so is fair both to other consumers and to the creators and producers of the music being taped.

The National Consumers League, therefore, respectfully urges this committee to pass S. 1739. Do not delay its consideration in the name of consumer protection.

Thank you.

[The prepared statement of Mr. King follows:]

Testimony of

Jane M. King
Deputy Director
National Consumers League

Mr. Chairman, on behalf of the National Consumers League, I want to thank you for inviting us to share our views today on S. 1739, the Home Audio Recording Act.

On April 21, 1986, we wrote a letter to Subcommittee Chairman Mathias to express our support for this legislation. I would ask, Mr. Chairman, that the letter be made a part of today's hearing record.

The National Consumers League has worked for economic and social justice throughout our 87 year history. We support this legislation because we believe it is consistent with our two fundamental goals: assuring economic justice in the marketplace and fair compensation for workers. The legislation before you today, to provide compensation to creators and producers of music, is consistent with these goals and is not, as some have suggested, anti-consumer.

Most people regard home taping and the technologies that make it possible as a wonderful opportunity for consumers; they can obtain prerecorded music without paying for it. After all, wouldn't we like to be able to freely duplicate many products on the market without paying for them? We know, however, that the benefits of such a marketplace are short term and illusory. Simply put, if we consumers aren't willing to pay a fair price for the goods and services we obtain, the producers will justifiably stop producing them and we will be the losers in the end.

The legislation now pending before the full Judiciary Committee is substantially different from the bill that was originally introduced. Although we supported the original version of S. 1739, we accept certain changes that have now been made and applaud others that have greatly improved the legislation.

Specifically, the proposed royalty on blank tape has been removed. The royalty will be placed only on equipment capable of direct recording and tape duplicating. A major improvement, made possible by new technologies, permits manufacturers who believe that their customers will not use the equipment for recording to avoid paying the royalty by placing an inexpensive "copy-code scanner" in the equipment. We believe this provides the equipment manufacturers and consumers in the marketplace with a clear choice which is to the consumer's benefit.

In addition, the Subcommittee adopted a distribution system for the royalty pool which will assure that substantial portions of the proceeds are used to develop new talent, thereby increasing consumer choices for music purchases. The distribution will be weighted in favor of recordings which are not high on the sales charts and will also provide greater compensation to composers, publishers and musicians.

The manufacturers of recording equipment are benefiting financially from the broad consumption of their products for the express purpose of home taping prerecorded music. In the name of the consumer, they are opposing this legislation. We believe that they are profiting substantially from the labors of the musicians and artists, but have failed to recognize their responsibility to compensate them in some way. In our view, consumers need both the hardware and the software. The equipment would be of little value to the consumers without prerecorded music.

The music industry is declining because of the growth in home taping. How do we know? We know because there have been 43% fewer new releases since 1978 and jobs have been lost. Consumers lose out when the variety of prerecorded music available to them is reduced.

Consumers also lose out when home taping results in reduced support for the more specialized forms of music, such as jazz, classical, folk and gospel records that lack mass market appeal.

Consumers of music lose out when the growth of home taping means record companies must raise their prices to those who buy their records because there are fewer sales over which the companies can spread their costs.

And consumers lose out when talented young men and women are discouraged from pursuing careers as musicians, vocalists or composers. If the creators of our music are not compensated for the fruits of their labors, they have less reason to share their talents. It is in our interest as consumers to assure them of adequate compensation for their creations.

We believe that the entire Nation benefits when Congress acts to uphold the principles of copyright. Our Constitution specifically recognizes the need for our Nation's copyright system to promote the arts. This system serves as a model to other countries around the world. Other countries have already enacted legislation similar to the bill we are discussing today. We must not let the United States fall any farther behind in upholding basic copyright principles.

Ironically, American music is one of the few industries that has a positive balance of trade. Continued erosion of the base which rewards American artists and musicians for the fruits of their labors will surely subvert this balance. The Japanese manufacturers of recording equipment profit from the creations of our artists, but they invest nothing in the new, talented musician who might be the next Aaron Copeland or the next Frank Sinatra. Consumers cannot afford to be as shortsighted and careless about the American music industry as the foreign manufacturers of recording equipment are willing to be.

American consumers have a finely developed sense of fairness. Asking those who copy prerecorded music to pay for the privilege of doing so is fair, both to other consumers and to the creators and producers of the music being taped. Consumers will support legislation that ensures a measure of compensation because they understand that getting goods for the cheapest price is not a good deal if it ends up sacrificing things worth paying for. Providing this compensation to creators and copyright owners may raise the price of equipment slightly, but it will help guarantee the continued quality, diversity and availability of the American music that people want to tape.

The National Consumers League therefore respectfully urges this Committee to pass S. 1739; do not delay its consideration in the name of consumer protection.

Senator MATHIAS. Thank you very much.

Ms. Cribb, you have a comment?

STATEMENT OF DICKSIE CRIBB

Ms. CRIBB. Senator, I appreciate being here today. I am Mrs. Kenneth Cribb from Spartanburg, SC, and a member of the board of the National Federation of Music Clubs representing South Carolina.

As Ms. Ward said, there are over 600,000 of us. We are the largest music philanthropic organization in the world. One thing that we did not really consider until some time ago—we are all consumers; we are all consumers.

When we talk of the consumers out there, we are talking about ourselves at the same time, but the reason we are here today is to preserve the property rights of our composers, our young musicians. We are not talking about the big record companies.

They have to exist; they have to make profits to be in business. But we are killing the creativity in America; we are killing it. Five records out of six lose money, and it is only the occasional hit record that takes care of all of the business.

Do you know what really amazed me? Mr. George David Weiss, who is president of the Songwriters Guild, told me, you know, I am scared; I do not want a big hit because that is when they really steal. I would like to get a little hit so that I can get some income coming in.

We are here today to protect the property rights, their God-given rights, as it is under our Constitution. We appreciate being here to represent the National Federation of Music Clubs.

One thing in closing, may I say. The home taping seemed so harmless 5 or 6 years ago, but you multiply it by hundreds of millions of copies a year and you are killing a business.

Senator MATHIAS. Thank you very much, Ms. Cribb.

Mr. Silbergeld, the Consumers Union publishes a very popular and well-used report, the Consumer Report, right?

Mr. SILBERGELD. We do.

Senator MATHIAS. Do you copyright that?

Mr. SILBERGELD. Absolutely.

Senator MATHIAS. Now, if somebody Xeroxes a page and distributes it, a nonmember, nonsubscriber, how do you feel about it?

Mr. SILBERGELD. Well, probably, we would rather have that person's subscription.

Senator MATHIAS. What do you do about it?

Mr. SILBERGELD. But there is a fair use doctrine which permits somebody to go to the library and use the library's copies, and if there is some brief excerpt that they want to carry to the store with them they can photocopy a page or a table. What we do, Senator, and I think what you are getting at, is we prohibit the commercial use of our ratings, for two reasons.

No. 1 is that extensive use, directly and lengthy quotation, is not fair use, but it is copying for commercial gain; more important, not for copyright reasons but because of our own noncommercialization. Such use is bound to—No. 1—distort the ratings by taking them out of context.

And No. 2, it is likely, and we believe very strongly likely, to create the impression that there is some connection between use and the advertiser. That is not the same thing as home copying which is for purposes other than to avoid purchase.

Senator MATHIAS. But you do assert your copyright interest?

Mr. SILBERGELD. Oh, yes.

Senator MATHIAS. And you do protect it?

Mr. SILBERGELD. Yes, indeed.

Senator MATHIAS. And do not misunderstand me; I am not critical of that. The Constitution provides for copyright protection and the laws implement copyright protection.

Mr. SILBERGELD. I absolutely agree, Senator. But the U.S. Government does not undertake that activity for us. We do it ourselves, and we do it in the case where a commercial party is violating our copyright for commercial gain, and we agree that that policy should be pursued with respect to copyrighted entertainment programs as well.

Senator MATHIAS. You do act under the provisions of the copyright laws, right?

Mr. SILBERGELD. Oh, yes.

Senator MATHIAS. That is really what we are talking about. What should the copyright law be with respect to recorded music?

Mr. SILBERGELD. Yes, but, Senator——

Senator MATHIAS. We are not talking about setting up any record police in which the government will specifically provide enforcement. It would still be up to the parties to enforce, but what should be the framework?

Mr. SILBERGELD. I suppose the equivalent would be if we came to the Congress and asked for a tax or a royalty on all library subscriptions to magazines available by private subscription and distribution to the copyright holders, because people go and read the magazine at the library.

Senator MATHIAS. Well, that has been talked about. It is not a novel idea.

Mr. SILBERGELD. I do not believe we would support it, though.

Senator MATHIAS. In some countries, that is in effect because library use is multiple use.

Mr. SILBERGELD. We believe it would reduce the support of our product.

Senator **Mathias**. Well, do you see any contradiction between the Consumer Union's efforts to control use of their own copyrighted output and your opposition to the recording industry's efforts in this respect?

Mr. **Silbergeld**. Not at all, Senator. Our assertion of our copyrights are—as I have described, I do not think they are at all parallel to S. 1739. I believe that S. 1739 clearly seeks to collect from everyone who owns a machine that is capable of an infringing a royalty to compensate for the infringing uses that are undertaken by a few.

Senator **Mathias**. Let me ask you one other question about the Consumer Report. Do you charge the same subscription to a library as you do to an individual homeowner?

Mr. **Silbergeld**. I believe that we do, yes.

Senator **Mathias**. You believe it or you know it?

Mr. **Silbergeld**. Well, I am not in the circulation department. It is my understanding that our rate is the same for all subscribers. I would be glad to supply that information for the record.

Senator **Mathias**. Would you supply that for the record?

Mr. **Silbergeld**. Certainly.

[Consumers Union charges the same subscription rate to all subscribers, whether individual or institution.]

Senator **Mathias**. There are, of course, many publications who do charge a higher rate for institutional users and institutional subscribers just because there will be, presumably, multiple readers.

Mr. Miller, Senate bill 1739, as reported by the subcommittee, includes several exemptions for nonprofit organizations and for equipment that cannot record or that can record only through a microphone.

If you do not think that these exemptions are broad enough to meet the needs of the blind consumers, do you have any suggestions that would improve this?

Mr. **Miller**. I was thinking of that with great interest during one of the earlier panels because it was not my privilege to hear the technical hearings some weeks ago about the encoders and decoders, and so forth.

The problem that most blind people encounter is even though there may be playing machines available for simply listening, for all of those uses that involve recording blind people have the same variety of needs.

If some of the solutions that have been talked about, like the use of the encoder and the decoder, et cetera—if these would avoid the critical problems we have outlined, such as the disproportionate impact of cost on people least able to afford the price, first of all, and the second one being whether there would be a workable exemption—and then, of course, the third point that this penalizes everyone—if these could be avoided by some other system, we would be obviously pleased to consider that.

The encoder/decoder system sounds to me as if it relates to just music and things like that. Most of the applications I have referred to do not refer to music. But, again, one of the earlier panelists indicated that most of the applications of recording do not relate to music uses either.

Senator **Mathias**. Well, as you can see from the language of the bill, there was an attempt on the part of the subcommittee to provide exemptions.

Mr. **Miller**. Right, and we genuinely do appreciate that.

Senator **Mathias**. We would be very open to your further suggestions as to proposals that would be, in your judgment, more effective.

Mr. **Miller**. Thank you. We will certainly give very serious consideration to anything we can pick up.

Senator **Mathias**. Mr. Yudkin, we have some conflict in testimony here. You said that you did not perceive a problem, or I think you said that.

Mr. **Yudkin**. Right.

Senator **Mathias**. Ms. King says that according to her information, there have been 43 percent fewer new releases since 1978. Now, leaving aside the loss of revenue, which I think is something which is hard to refute—but leaving that aside, what about this question of the 43 percent fewer releases?

Mr. **Yudkin**. Well, I was thinking, you know, when you get a morning newspaper—you must get the Baltimore Sun or the Washington Post—you know, if you had to buy a copy, you buy a copy for everybody in your office. You know, if your secretary picks it up, you are violating the copyright.

You bought the Washington Post or the Baltimore Sun. Everybody in your office should buy a copy of it. Anybody else who looks at it is really violating it. But if you go into the music part, there are so many aspects of it.

There are concerts. Listening to the music encourages you to go to a concert and want to, you know, spend more money on concert tickets. It gets you to watch MTV and watch the video of it. By watching MTV, you watch the commercials of it that go along with MTV and help pay for MTV.

There are not only records. You know, maybe record sales are going down, but people are buying compact discs; people are buying tapes.

The record stores I talked to—the man from Peppermint Records does not seem to be hurting in sales. The record stores in Louisville, KY, that I go to seem to be doing well.

I do not see how there is this great loss—maybe in one aspect of it, but certainly the concert business is picking up and MTV business.

I think the consumers want something fair. They want to be able to—if you are doing it for your own use, fine. If you are out there doing it for commercial use and you have a big factory like they were talking about in North and South Carolina with people making hundreds of copies, let us stop them.

I agree that that is something that should be stopped, but let us promote music. I think the way it is now, the administration is not supporting this bill. I think they have seen that a tax is not the way. Let us think of some other ways of trying to help.

Senator **Mathias**. But given the testimony of Ms. Ward and Ms. Cribb, is not the problem a little more complex than the way you present it? It may be that volume sales are holding up, but let us leave that question aside. The question is diversity.

What Ms. King said was there were 43 percent fewer releases. That goes to the question of diversity; it goes to the question of choices available to the public. It goes to the question of individual taste in music.

The giants can be pressing a number of albums but what about the smaller outfits? What about the individual composers, and, as Ms. Cribb points out the younger composers? What opportunities are available for diversity and creativity? Does that appear to you as a problem?

Mr. **Yudkin**. That would be a problem, but I do not see it is related to people copying at home. I just do not see that you have copied something else off the radio that is going to stop new artists from coming out there.

Senator **Mathias**. So you do not see the causal relationship?

Mr. **Yudkin**. I do not see a causal relationship. If there is less music out there, I think we should try to promote it, but I do not see that copying is the cause of it.

Senator **Mathias**. Then maybe I should turn to Ms. King and see what her comment is.

How do you respond?

Ms. **King**. Copying does probably expand the use of music. I would like to give an example because I did some checking in the past week in my own household and among friends of my 17-year-old. It is clear, at least in that age group, that there is a great deal of copying among friends of one record.

In other words, if one person buys a record, it will be shared with five or six others. When my daughter gets into college, I have a feeling it will be 10 others.

What this does to original music is reduce the volume of records sold among records that are being copied on blank tapes. As a consequence, the investment of the entire industry in the less popular forms is shrinking.

If you go into a record store now and look for classical music, you will find less American production. The same thing applies in any of the so-called speciality music, such as folk, jazz, and so forth.

So that is our conclusion, that we are shrinking the base of possibilities, and also, simply in terms of property rights, denying the remuneration to those who created the music. I think we are denying the rights of creators.

Senator **Mathias**. It seems to me that latter point is very hard to escape. If you make a tape, you are denying the owner of the copyright a legitimate return on the ownership of the copyright.

But leaving that aside for the purposes of this conversation, I think the argument you make is an interesting one. The reduction of the base affects the interests of consumers as well as the interests of the copyright owners, and it does go to the question of diversity.

Ms. Ward, you have related our musical heritage to the encouragement that the copyright system has provided. Lincoln once said that the intellectual property system added the fuel of interest to the fire of genius. I think that is a very concise and neat way to express it.

There is also, of course, encouragement which comes from organizations such as the National Federation of Music Clubs. In the last panel, Mr. Roach mentioned copyright education. Has your organization considered, with its 600,000 members, a program of copyright education?

We are approaching, next year, the bicentennial of the Constitution. One feature of that is, of course, the bicentennial of this whole system of patent and copyright protection which for 200 years has been a part of our laws.

It offers an interesting opportunity to educate the public to the fact that there is in this country, and not in every country, a respect for the creator of ideas and of artistic productions.

We not only respect the right of property in a piece of land or in a cow or in an automobile, but also we push it to one higher level of society and of civilization, and we respect ideas as well as material property.

So I suggest that to you as a project to coincide with our celebration of the bicentennial.

Ms. **Ward**. That is most interesting, Senator Mathias, and we would like to know further about that because during the bicentennial year in 1976, we sponsored a big project with which I am sure you are familiar.

Every State in the United States presented a program at the Kennedy Center in the order that that State came into the Union, and the music presented on the program was indigenous to the State.

So I think that this is most interesting and we would like to hear further about that, and I am sure we might implement something.

Senator **Mathias**. I would be personally happy to provide any information or help that I could.

Ms. **Ward**. Wonderful.

Senator **Mathias**. But I think 1987, as the bicentennial of the Constitution, does provide us an opportunity to appreciate all the benefits that the Constitution confers. Not the least of which is the protection of intellectual property.

Ms. **Ward**. Thank you.

Senator **Mathias**. Ms. Cribb?

Ms. **Cribb**. Senator Mathias, may I say one thing? So much of the erosion of the intellectual property of the individual is done unknowingly. So many of our members themselves, members of the federation who promote the artist, who promote the composer, who promote the culture of this country, themselves say, you know, I did not realize what I was doing.

This wonderful record had come out, and she said it was so wonderful, I made six copies to give to my friends. Now, these are people who are trying to protect the copyright laws. It is reeducation, it is education, it is protection, and I think that is a wonderful idea. But it is being done sometimes—people do not realize what they are doing.

Piracy is bad, but it is the erosion by some people who are doing it innocently at times.

Senator **Mathias**. I think that is very true. I think you might even find Members of the U.S. Senate who are inadvertently guilty of that from time to time, and so, I think that it could be a good project for the bicentennial period.

Well, we thank you all very much for being here and we will appreciate the followup that we have requested from several of you.

Our fourth panel, and final panel: Mr. Niles Borop, of Nashville, and Mr. Jim Ritchey, of Greensboro, NC.

Mr. Borop.

STATEMENT OF A PANEL CONSISTING OF NILES A. BOROP III, MEMBER, SONGWRITERS GUILD OF AMERICA, NASHVILLE, TN; AND JIM RITCHEY, MEMBER, AMERICAN SOCIETY OF COMPOSERS, AUTHORS, AND PUBLISHERS, GREENSBORO, NC

Mr. Borop. Good afternoon, Senator Mathias and members of the committee. As you know, my name is Niles Borop, and I am pleased to be here today to testify in support of S. 1739, the Home Audio Recording Act.

In the interests of time, I would like to submit my written testimony for the record and briefly state the two key points I would like you to consider this afternoon.

Senator Mathias. Your full statement will be included in the record as if it were read.

Mr. Borop. First, I am a very successful songwriter. Churches across the country know and sing my songs. Singers have recorded over 150 of my songs and performed them on national television.

For the past 2 years, I was nominated gospel songwriter of the year, and this year my song "Via Dolorosa" won song of the year in Christian music. But despite this success, my income alone cannot support my wife and me.

My second point is that since I am paid for my work only when the records containing my songs are sold, home taping robs me of royalties. Since every dime counts in my household, this can add up quickly.

I love writing songs and want to be able to continue in this profession for many years to come. What S. 1739 does is simply gives me a chance to get paid for my work. I urge your favorable consideration of this legislation and look forward to answering any questions you might have.

Thank you.

[The prepared statement of Mr. Borop follows:]

STATEMENT OF NILES A. BOROP III
before the
Senate Judiciary Committee
Re The Home Audio Recording Act
August 4, 1986

My name is Niles A. Borop III, and I am honored to have the opportunity to testify in support of the Home Audio Recording Act. That legislation has been endorsed by every major songwriters' organization in the country, from the Songwriters Guild of America to the Nashville Songwriters Association International to the National Academy of Songwriters, as well as by innumerable associations of which songwriters are prominent members, like the Country Music Association, the Gospel Music Association, Meet the Composer, the National Academy of Popular Music and the Nashville Music Association, to name but a few.

As a member of the Songwriters Guild of America, I am pleased to appear as a representative of that organization, but I also want to share with you my personal story of how home taping affects my ability to make a career in music. Let me first tell you just a little bit about myself.

I am the son of Dr. and Mrs. Niles A. Borop Jr. of Aiken, South Carolina, where I was born and raised. After graduating with honors from Mercer University in Macon, Georgia, I attended Vanderbilt University in Nashville, Tennessee where I earned my Master of Divinity Degree in 1981. Shortly after I graduated, I became an ordained minister. After I graduated Vanderbilt, I also became a professional songwriter. I wrote country songs for Acuff-Rose Music in Nashville, TN for one year and for the last four and one half years I have been an exclusive songwriter for the Word Music Group. Word Records and Music is the world's largest publisher and recorder of Christian music. I am now one of their most successful songwriters.

I am one of only a handful of people in this country who is able to be a full time songwriter in the field of Christian music. For each of the last two years, I have been nominated as Gospel Songwriter of the Year and I have had songs nominated for Song Of The Year in Christian music. This year my song "VIA DOLOROSA" won Song Of The Year in Christian music. Within the last three years, I have had over one hundred and fifty of my songs recorded.

I am proud of my accomplishments -- but whatever success I have had must be tempered by the fact that I am able to write full time only because my wife and I have not had children and because my wife works full time to support us. Until this year, including the year I was first nominated for Songwriter Of The Year, I never earned more than slightly over five thousand dollars a year.

Home taping greatly affects me, for I am compensated for my efforts only when the records containing my songs are sold. When albums of my songs are borrowed and home taped, or home taped and given away to friends, the royalties I lose can add up quickly.

Unfortunately, thousands of people like to home tape our Christian music albums and give them away to friends as a way of sharing their beliefs or as a way of evangelism. I have run into this situation many times. When I have shared with these people that what they are doing deprives creative people of rightful income, these people have responded with comments like, "I bought the record so I can do what I want with it," or "Songwriters and recording artists are rich so my making tapes to give away won't hurt them", and even "The writers and artists ought to thank me for taping their record to give away because the person I give the tape to might like them after they hear the tape."

Perhaps if it were only a few who were engaging in home taping it wouldn't be a major problem -- but millions of people across the country are doing it! And the cumulative impact of that can be devastating!

When the average writer like me makes five thousand dollars a year, every penny counts. If the home taping of my music only amounts to three hundred dollars in one year, that may not seem like much on the surface, but that is a month's rent or groceries lost, that is precious income I need in order to simply survive as a writer.

When I first joined Word Music as a writer in 1982, Word Records had around one hundred and thirty artists who recorded for them. Just four years later, they have only some 70 artists on their roster. Although Word has numerous successful artists, a mere handful of them produce most of the income, and their success subsidizes the work of numerous people whose product is not making back the money it costs to produce their albums. Virtually all of Word's albums are home taped, but the albums of the more successful artists are home taped more often. Obviously this hurts the record company, the recording artists, the songwriters, the producers, and everyone else involved with the record, for it chops away little-by-little at their income. But oddly enough, it hurts consumers even more -- for they are deprived of the opportunity to hear new artists and the songs they would have recorded. Those who like less commercial forms of music also lose their chance to hear their favorite artists, for the record company can no longer afford to record them.

Within the last two years, I have had numerous opportunities to speak to church youth groups throughout South Carolina and Tennessee. On those occasions where I spoke about Contemporary Christian music, I asked the young people to bring their records and tapes to the meeting so I could see who they are listening to. On every occasion, blank tapes with home recordings have been brought to the gatherings. Recently, at the First Baptist Church in Aiken, South Carolina, I was overwhelmed when the young people brought in sixteen different home taped recordings of records borrowed from friends, and only one cassette tape actually bought from a record store. I asked the group if they buy the albums or tapes and make these copies for their personal use. They responded that NO, they each bought a record and passed it around to friends to record, because it was cheaper that way. I have understood for a long time that there is a home taping problem but this experience hammered home how real it is and that it does affect me.

I appreciate the fact that I have received many letters and phone calls expressing the impact of what I've written on people's lives. I am honored that churches across our country know and sing my songs. I am excited about all of that, but I would also like to eat, pay my rent and support my wife. Making as little as I do, every penny counts and even a small amount can have a huge impact on my life and my ability to contribute to the support of my family.

Each person home taping is like a tiny crack in a reservoir. It doesn't take too many cracks for the dam to burst. It doesn't take that many people home taping to cause a songwriter's career to collapse due to economic pressures.

I appeal to this Committee to enact a fair way for me and others like me to receive at least something of what we are entitled to, so that we can share in the income derived from the use of our copyrighted works. The way proposed in S. 1739 is a logical solution. It is a fair solution. I hope that you will seriously consider it.

Thank you.

Senator MATHIAS. Thank you very much, Mr. Borop.

Mr. Ritchey.

STATEMENT OF JIM RITCHEY

Mr. RITCHEY. Thank you, Mr. Chairman. How much time do I have?

Senator MATHIAS. Four minutes.

Mr. RITCHEY. Four minutes.

Mr. Chairman, members of the committee, my name is Jim Ritchey and I am one-half of the team of Ritchey and Fleming, of Greensboro, NC. The other half of the team is my wife, BeJae Fleming.

I am a member of the American Society of Composers, Authors and Publishers, and we make our living composing music and performing in clubs and concerts around the country. In fact, one of my original songs, "Tennessee Bottle," has been recorded by Kenny Rogers on his album "The Gambler," which means that I could possibly benefit from this legislation if it passes.

Now, you probably heard that the music industry supports and wants you to pass S. 1739, but that is not absolutely true. Only a part of the music industry wants this bill passed—the gaint labels and the superstar performers.

A large segment of the music industry, we independent composers and performers, oppose S. 1739. You have heard that the American Society of Composers, Authors and Publishers supports S. 1739. As a dues-paying member of that organization, I do not believe that it speaks for the majority of its members on this issue.

I believe I speak for thousands of independent members of the music industry when I say that we are against S. 1739. I am a professional musician and songwriter and I oppose the bill, as do other independent members of the music industry, and we urge you to oppose it, and I will tell you why.

I have studied the distribution scheme and I am convinced that if ever a piece of legislation bears out the old lament that the rich get richer and the poor get poorer, S. 1739 is it.

Most of the little guys of the music industry will never see any of the millions of dollars that the consumers will end up paying if the bill passes. The lion's share of the funds raised by the tax will be distrubuted according to record sales and airplay, and the big record labels will not record most of us so that our records can be sold or given for airplay to the radio stations.

But we will still have to pay more for the audio recorders that we buy in order to record our own music during the creative process. The net result is that we will be paying a tax, a royalty, to the big labels that will not even talk to us just for the privilege of recording our own music.

The 2 percent of the royalty tax to be given to the Musical Arts Endowment is a nice idea, but is is not practical. It will have no practical effect on encouraging struggling composers or performers, or promoting their music.

The 2 percent of the royalty tax that is raised by this bill, once it is trickled through a bureaucracy and it has been diminished by administrative costs, would amount to pennies, at best, for the average struggling artist, and we want our work to be heard and appreciated, not subsidized by a private tax.

It seems to me that taping our music is just about the biggest compliment the public can pay us. I do not want someone doing it and selling the tape to make money off our music. That is piracy, and it is illegal; it is abhorrent to me and I wish that you would take the steps to beef up the antipiracy laws that are already on the books. But we do not need more laws; we need to enforce the ones we already have.

Someone else, when they tape one of our records, may give it to someone who had not ordinarily or otherwise heard of Ritchey and Fleming, and that is promoting music not by a million-dollar aid campaign, but by people who pass it along for the pleasure of putting our music into circulation.

So if you members of the committee decide to go ahead and pass this tax and your people back home ask you why you did such, please do not tell them you passed it to help the music industry because I do not want it and neither do thousands of other musicians and songwriters.

I write music, I perform it; it is my life's work. I am opposed to the bill, and I would be happy to answer any questions that you have.

[The prepared statement of Mr. Ritchey follows:]

TESTIMONY OF JIM RITCHEY BEFORE THE SENATE JUDICIARY COMMITTEE ON S.1739

AUGUST 4, 1985

Mr. Chairman, Members of the Committee.

My name is Jim Ritchey and I am one-half of the team of Ritchey and Fleming of Greensboro, North Carolina. The other half of the team is my wife, BeJae Fleming.

We are members of the American Society of Composers, Authors and Publishers (ASCAP), and we make our living composing music and performing in clubs and at concerts around the country. In fact, one of my original songs, "Tennessee Bottle," has been recorded by Kenny Rogers on his album, "The Gambler," and we recently completed a successful engagement at a club just outside Washington.

You probably have heard that the music industry supports and wants you to pass S.1739, the Home Audio Recording Act. That is not true!

Only a part of the music industry wants this bill passed -- the giant labels and super-star performers or composers. They are the ones that will benefit from it to the tune of tens or hundreds of millions of dollars. Dollars taken from the consumer's pocket.

But to a large segment of the music industry -- we independent composers and performers -- S.1739, the audio royalty tax bill is just a bad idea built on some false assumptions.

You have heard that the American Society of Composers, Authors and Publishers supports S.1739. As a dues-paying member of that organization I do not believe that it speaks for the majority of its members on this issue.

I believe I do speak for thousands of independent members of the music industry when I say that we are against S.1739. May I take the liberty of repeating that so that there is no chance of misunderstanding. I am a professional member of the music industry and I oppose S.1739, as do other independent members of the music industry. And we urge you to oppose it.

I'll tell you why. I have studied the distribution scheme which has been added to this bill and I am convinced that if ever a piece of legislation bears out the old lament, "The rich get richer and the poor get poorer," S.1739 is it. The little guys of the music industry like me will never see any of the millions of dollars that music consumers will end up paying if this bill passes. The lion's share of the funds raised by this royalty tax will be distributed according to record sales and air-play. The big labels won't record most of us so that our records can be sold or given air play by the radio stations.

But you can bet we will have to pay more for the tape recorder we buy to record our own music during the creative process. You know, we musicians and composers use recorders and blank tape, not only for composing our own original music, but also for distributing it -- making demo tapes for radio stations and record labels -- in the hope of having our music eventually heard by the public. The net result of S.1739 will be that we'll pay the royalty tax to the big labels that won't talk to us, just for the privilege of recording our own music.

There are no two-ways about it -- to paraphrase the lyrics of a popular song, the giant labels and superstars will get the consumer's gold mine while the independent members of the music industry will get the shaft.

The two per cent of the royalty tax that is to be given to a "Musical Arts Endowment" is a nice idea that will have no practical effect on encouraging struggling composers and performers or promoting their music. Two per cent of the royalty taxes raised by this bill, once it has trickled through a federal bureaucracy, and has been diminished by administrative costs, would amount to pennies at best for the average struggling artist. We want our work to be heard and appreciated, but not subsidized by a private tax like S.1739.

It seems to me that taping my music is just about the biggest compliment the public can pay me. I don't want someone doing it and then selling that tape to make money off my music. That's piracy -- that is illegal, it is abhorrent to me, and I wish you would take whatever steps are necessary to beef up the enforcement of the anti-piracy laws that are already on the books. We don't need to pass new laws. We do need to enforce the ones we already have.

But this royalty tax bill you are considering, S.1739, is not an anti-piracy bill -- it's an anti-people bill. If someone tapes our music for their personal listening pleasure, someone else may hear that tape who otherwise had not heard of Ritchey and Fleming. That's what I call promoting music -- not by the million dollar ad campaigns of the big labels who usually won't even listen to us -- but by the little people who are doing it not to make money but just for the pleasure of putting my music into circulation. When I think about it, that's sweet music to my ears.

So if you members of the Committee decide to go ahead and pass this royalty tax -- and if your people back home ask you why you did such a thing, please don't tell them you passed it to help the music industry. Because I don't want it, and neither do thousands of other independents of the music industry.

I am as much a part of the music industry as anyone else in this room. I write music. I perform it. It is my life's work. And I am opposed to this bill.

I will be happy to try to answer any questions the Committee might have.

Senator MATHIAS. Thank you very much.

Mr. RITCHEY. You are welcome.

Senator MATHIAS. Mr. Borop, in the part of your statement that you did not read, you noted that when you joined Word Music as a writer in 1982, Word Records had around 130 artists who recorded, but that 4 years later they were down to less than half; they were down to about 70.

Mr. BOROP. Yes, sir.

Senator MATHIAS. In your judgment, what is the loss of diversity of music that is represented by this decrease in the number of recording artists?

Mr. BOROP. What you find in contemporary Christian music is a huge array; whatever is found within the realm of secular music is found in Christian music because the only difference between Christian music and secular music is the lyric content.

So what you find is more—country gospel, in particular, has had a very, very bleak showing in Christian music. Southern gospel groups are more and more having to turn to customized albums as opposed to major-label albums, as the major labels cut back.

Virtually every facet, especially the old-time inspirational Tennessee Ernie Ford type of music, is greatly affected by this because the market is much smaller. The Amy Grants and the Sandy Paddys who make the majority of the income are subsidizing the recordings of those artists who do not make near as much on their album sales.

In fact, most of their albums do not make back the money, so the albums that do make the money need to subsidize those. But as home taping begins to erode, the record companies do not have the resources there to subsidize those types of records.

Senator MATHIAS. Let me ask Mr. Ritchey if he sees any causual relationship between the recording practices of today and the decrease in the number of recording artists that Mr. Borop has reported.

Mr. RITCHEY. I do not see a relationship between home taping and the reduction of the number of artists. I do see the major labels reducing the number of artists that they carry in order to maximize their profits.

Senator MATHIAS. Would that include an organization such as Word Music?

Mr. RITCHEY. Word Music is a major label in the Christian music sector. I do not know what its position is in the overall scheme of California record companies.

Senator MATHIAS. But that presents us with a factual question of why Word Music reduced the number of recording artists.

Mr. RITCHEY. It sounds to me like they made a decision based on the number of records that were being sold and decided that some of the other artists were not selling enough records.

Now, I do not see any correlation there with home taping whatsoever. That sounds like a business decision to me, based on marketing concerns.

Senator MATHIAS. Let me ask Mr. Borop to comment on that question because in a later part of his written statement, he referred to discussions he had with groups of young people in South Carolina and Tennessee about their recording habits.

What light can you shed on this question of fact?

Mr. BOROP. Well, sir, I always liked to believe that the home taping problem was not a major issue and that certainly it was not affecting me as a writer. I am certainly every bit for the consumer. That is why I write; that is why I create, so that other people may be able to benefit from what I do.

All I ask in return is simply to be able to be paid what the law says that I am allowed to be paid. Home taping does not allow that.

I went to First Baptist Church in Aiken, SC, to speak to their youth group and asked them to bring their recordings in order that I might see who they are listening to and so I might address them more specifically.

Well, what I found was that they brought 17 tapes, 16 of which were home taped. Now, I asked them, did they buy the records and then tape these tapes for their personal use, and they said no. What we do is each buy one record and we pass it around among friends. You know, it is cheaper that way.

That shocked me. It shocked me into awareness that even in my home town this type of thing is going on. If it is on that small of a scale because it is a small scale—if it is happening across the country, it is the same type of impact on my career as a tape pirate is.

The only difference is with a tape pirate, it is a centralized location; you can somehow catch that person. With the home taper, obviously most of the time for more innocent reasons, there is no way to enforce the law.

What this bill does is simply offer a solution in which I might be able to receive some portion of the income to which I am already entitled.

Senator MATHIAS. Of course, one of the reasons it is cheaper to do it that way is because there is no payment of any compensation to the composer or to the artist for that particular use of their talents.

Mr. BOROP. Right. If I may make a comment, one of the things I would like to express from a personal experience is that all I do is write. I am not a performer-writer, I am not an arranger-writer, I am not a producer-writer. My income comes solely from writing songs.

Now, for those who can make their income from other ways, the home-taping issue may not be quite as significant an issue because it is a secondary means of income for them. But for me, it is a primary source of income.

Even if I make only $300 or $400 extra a year, that can make a tremendous difference because the average songwriter makes only $5,000 a year in this country. The fact is that I am in that category.

The year I was first nominated for songwriter of the year, I only earned $5,000, and if I could have gained an extra $150, $200, $300 from this bill, it could have greatly affected my life. It could be an extra month's rent; it could be groceries.

The figure, when it gets down to the bottom line, to songwriters is very significant, even if it seems to be a small amount of money in quoting figures.

Senator MATHIAS. Well, now, Mr. Ritchey, I believe you said that you did not care if people taped your music and distributed it among their friends.

Mr. RITCHEY. No; I do not.

Senator MATHIAS. But as you hear from Mr. Borop and as this committee has heard on previous occasions, there are other composers who do feel very strongly about it. Since they do feel strongly about it and since, under the principles of our law, they have a right to feel strongly about it, how would you suggest that they be compensated for home taping, for the use of their intellectual creations?

Mr. RITCHEY. First of all, Senator, I would suggest that they consider the other possibilities. There is going to be interest in this gentleman's music because——

Senator MATHIAS. What are the other possibilities?

Mr. RITCHEY. The other possibilities are that his sales are going to increase because people are listening to this music that has been distributed through home taping. He is building, as do all composers—we build our popularity based on the number of people who actually get to hear the music. That is why it is played on the radio.

Even though we are paid for every time it is played by home taping, we are not paid for every time it is played by the person who purchases the album. I mean, all of this is important, all of this exposure is very important, especially to a small artist. It is very important.

The only way that we get to be big artists is for people to know who we are, and the way that happens is exposure. The exposure that we get from these tapes circulating is good.

Senator MATHIAS. So you would say just forget about what you should have earned on these performances of your works. Just consider it as what the retail industry calls a "loss leader."

Mr. RITCHEY. No, sir. I am saying do not think that just because this person taped the album that they would have bought it. Chances are they might not have bought it anyway, and they are getting to hear something that you want them to hear, and that is a very important part of what we do, is getting the music out.

It does not mean necessarily that an album sale was lost there.

Senator MATHIAS. I follow that logic and I think that is probably true that everyone who tapes would not necessarily have purchased the music that be taped. However, that does not answer the question of the use.

If you take some large material object like an automobile, if someone uses your automobile, just uses it without your permission and without compensating you, you have a right to feel aggrieved, do you not? That is your property.

Whether or not they could have gone out and bought another automobile chances are they would not have bought another automobile if they could have used yours.

Mr. RITCHEY. Well, people are not taking—I put the music out in the public domain. I did not put my automobile out in the street with the keys in it. You know, it is a difference between theft and private use, as we are concerned.

Senator **Mathias**. Well, now I think you have touched a very critical point here when you say that you put the music out in the public domain. The copyright laws are intended to protect property for a period of time before it goes into the public domain.

There is a time when it goes into the public domain, but during the time when it is subject to copyright protection, it is not in the public domain.

Mr. **Ritchey**. Well, Senator, I am not a lawyer, so I admit that I did not use the correct usage of public domain. But at any rate, I am in favor of copyright as an idea and as a law.

I believe that there are other considerations that are practical considerations that tie in with personal use. I am not for piracy in any form, but there is a certain kind of exchange that goes on among people who love music.

People are not only trading the music around; along with that, they are giving a part of themselves. They are telling this other person, you know, this is the way I feel, this is the way I think, this is important to me; I want to share it with you.

That is very important to composers to know that that is happening.

Mr. **Borop**. Senator.

Senator **Mathias**. Yes; Mr. Borop.

Mr. **Borop**. I would like to respond to that. Yes; it is very important to me. I have gotten hundreds of letters and church bulletins and notes of appreciation of how my song touched someone's life.

What that makes me feel is even stronger about the position of this bill because without this bill, my ability to make a living is severely hampered. Therefore, I would not be able to continue to write songs that hopefully will, in the future, continue to touch those very same lives.

It is frustrating when I have to hear the other side. Of course, I want to touch people's lives, but in order to continue to be able to do that, I have to have an opportunity to make what the law already says that I can make.

Senator **Mathias**. Mr. Ritchey, assume that it is good for Mr. Borop if somebody tapes his song, from the subjective point of view that his music is being heard and his message is being broadcast. How is that going to help him materially as a composer?

Let's take, for example, an unauthorized copy of a Patsy Cline record. Her name will be mentioned as the more prominent contributor to that recording, and her voice will be heard by all. But, Mr. Borop, as the composer, may be ignored in the taping process. There is no recognition given to the composer. There is no label on that tape, "composed by Borop." All they will recognize is Patsy Cline's voice.

They may go out and buy another Patsy Cline record, but they do not necessarily look for a Borop composition. So how does that help him, aside from the highly subjective satisfaction that more people have heard his message?

Mr. **Ritchey**. There is no guarantee that they will not pick up the album jacket at the record store and see that information.

Senator **Mathias**. There is no guarantee that they will not, but there is no guarantee that they will, either.

Mr. **Ritchey**. No; that is true.

Senator MATHIAS. In fact, the chances are very much against it.

Let me ask you this question, too. You were critical of the distribution scheme. Admittedly, that is a difficult problem. How do you distribute these funds once they are collected so that it is fairly and equitably distributed?

The amendments that the subcommittee adopted provide for an 80-20 plan for smaller artists, and smaller operations. That plan, of course, includes a scheme that ensures that all who participate in creating copyrighted music earn a share.

Then we have provided for 2 percent of accumulated royalties to be allocated to the National Endowment for the Arts. Our intent is that those funds will be used to stimulate creativity among aspiring young artists.

So, this may not be a perfect scheme, but it is an attempt to be fair in distributing the moneys that are accumulated as equitably as possible. If you have a better method of distribution, we would be glad to hear it.

Mr. RITCHEY. I have not come up with a better distribution plan, but let me say that the 80-20 part to which you prefer is part of the sound recording fund, and that split is going to go to the record company.

Mr. Borop's part comes out of the musical work fund, which is a much smaller—it amounts to like 22.5 percent of the total, divided 50-50 between the music publisher and the writer.

Senator MATHIAS. That is the nub of your objection?

Mr. RITCHEY. No, sir; that is not the nub of my objection. The nub of my objection is that it is not equitable distribution because if you look at this carefully, Michael Jackson, Bruce Springsteen, and Madonna are going to be doing very well out of this as artists and composers.

The Christian artists are going to be placed in the incentive class unless Amy Grant happens to have a megahit. I mean, the figures here are based on total sales and airplay, and we are talking about very, very small amounts of money left over.

I mean, if you take the whole Christian catalog and put it up against—I mean sales—against one song by a major artist, I do not have specific figures to back myself up, but I would guess that an artist like Bruce Springsteen could probably outsell the entire Christian catalog on one song. That is slightly less than an educated guess.

But I do not think that people like my colleague here are the ones who are going to benefit from this.

Senator MATHIAS. If we altered that distribution scheme so that a little more went to the one side and a little less to the other, would you feel better about it?

Mr. RITCHEY. No, sir.

Senator MATHIAS. I had a feeling you would not. [Laughter.]

Mr. RITCHEY. Well, can I digress just for a moment? I need to tell you where my feelings come from on this. The first time I heard about this legislation, I received a package of material from ASCAP, of which I am a publisher member and a writer member, and I respect the organization highly and have nothing against them.

But they wanted me as a member to write the Congressman in my district and the Senators in my State in support of the bill. When I saw that, I objected to it not as a musician, but as a citizen.

I mean, I had a terrible feeling, an immediate reaction, because I felt like there was an unfair, arbitrary tax about to be foisted upon people who were not going to benefit from it. I did not like the idea.

It occurred to me as I read the thing that I stood to benefit. I mean, I had a song on an album that sold, I do not know, 4 to 5 million copies. It is still in print; it is still selling. I am going to make a few bucks if this thing passes.

I might even make $300 or $400, which is unlikely, but if Mr. Borop thinks he could make that much, I could make that much, too.

It is very difficult for me; I am on the line here. I am going up against a major part of the industry that I am a part of. I am going against an association that I respect because I have strong—forgive the use of this word, but it becomes a moral issue with me because there is something that is violating my rights as a citizen here.

Senator MATHIAS. Let me take you back to the automobile example we discussed earlier. Is that not a moral issue if somebody uses your car and does not pay you any compensation for its use? As a citizen, do you resent that?

Mr. RITCHEY. Well, to me, you have not seen my car, Senator. [Laughter.]

Senator MATHIAS. You have not seen mine. [Laughter.]

Mr. RITCHEY. Forgive me. I am really having a hard time tying——

Senator MATHIAS. Well, you just give me an answer to the question and then I will try to tie it together.

Mr. RITCHEY. I am sure you will do an excellent job, too.

I do not want anybody stealing my car.

Senator MATHIAS. I did not say stealing. Let us keep those harsh words out of it. Let us just say somebody takes your car and drives it 100 miles and brings it back to you.

Mr. RITCHEY. Well, if I find it is gone, I am going to think it is stolen, so it is, you know——

Senator MATHIAS. You do not quite want to say it, but I think you think you ought to be compensated for the use of that car. No. 1, you would rather not have them borrow it. No. 2, if they do, you think you need to be compensated. Am I wrong?

Mr. RITCHEY. I will say that I would rather not have them borrow it, and when that happens I will have to make up my mind on the other part of that.

Senator MATHIAS. That is how Mr. Borop feels about his song; he would rather not have them borrow it.

Mr. RITCHEY. I know how Mr. Borop feels about his songs.

Senator MATHIAS. What is the difference in terms of property under the Constitution of the United States between your automobile and your intellectual creation as long as the copyright is in effect?

Mr. RITCHEY. Well, our creations exist——

Senator MATHIAS. That is the hard rock on which we find ourselves.

Mr. **Ritchey**. Well, I have a lot more control over my automobile than I do all of my songs. I have not had near the number of songs that this gentleman has recorded, but I have had a few, and there is not just one of them—I mean, this song—I am sorry. I just cannot make a connection with your analogy, sir. It is very difficult for me.

Senator **Mathias**. Well, that, I think, is the problem here.

Mr. **Ritchey**. I do not see my songs as property.

Senator **Mathias**. You do not view a copyrighted production as property?

Mr. **Ritchey**. Well, I prefer not to view my own music as property, but I suppose if I were to look at it from a strictly legal standpoint, I would have to do that.

Senator **Mathias**. Well, that is how we have to look at it.

Mr. **Ritchey**. I understand that.

Senator **Mathias**. Yes.

Mr. **Ritchey**. But you have to understand that there is another side to this. I mean, being a creator causes emotional concerns that lots of people who produce products do not have to deal with.

I mean, to me, with many of my songs, I will have to say this in all honesty. If it is a choice between people hearing this song and hearing what I want them to hear and my getting paid for it, there are certain songs—not all of my songs, but some of my songs—that I would have to say, go ahead, listen to it, you know, and I will forgo the money, if that is the choice I am forced to make.

I do not really feel like that is the choice.

Senator **Mathias**. But you are implying that you have a choice, and the situation with which we are faced generally is that Mr. Borop does not have a choice and other composers do not have a choice.

That is really why we are here, to see if there is any way we can give them a choice.

I thank you both for coming here today. This kind of conversation is very helpful in trying to understand all sides of this difficult question.

Mr. **Ritchey**. Senator, I am sorry; forgive me. I just have one more thing to add. The reason I got a song on the Kenny Rogers album in the first place was because a tape circulated without my knowledge.

I gave a man a tape at a party; a man that I had never met before that I liked and who liked me. I gave him a tape and about 6 months later I got a telephone call that said Kenny cut your song.

Well, you know, that tape drifted from hand to hand. It was copyrighted material because it was copyrighted——

Senator **Mathias**. Was it a commercial tape that you gave him?

Mr. **Ritchey**. The tape and the song, because the minute I affixed the copyright symbol to the tape, it was a copyrighted piece of material.

Senator **Mathias**. No; was it just a home cassette or was it a commercial cassette?

Mr. **Ritchey**. It was a home cassette, but it was copyrighted material. One song generated over $100,000 just by being on the album. It was not a hit. It got very little airplay, but this is just another illustration that this circulating music does marvelous things.

Senator MATHIAS. Of course, when you provided a home cassette, maybe they felt that you were saying go thou and do likewise.

Mr. RITCHEY. It is possible that they were.

Senator MATHIAS. Mr. Borop.

Mr. BOROP. I find what he is saying highly, highly misleading. As a songwriter, I will make demonstration recordings of my songs to submit to artists. That is standard music business and industry practice.

We are not paid for those. Those are the ways in which we show the song to the artist for their consideration. The fact that he already said that it was not a tape that was already for sale or that it was his own tape that he is using as a promotional copy—I think it is a very misleading thing because this was not a home-taped recording. It was a demonstration recording, and there is a huge difference between the two.

Mr. RITCHEY. Senator, all of our demonstration recordings that we use to get the performances that we make our livelihood from are home-produced.

Mr. BOROP. And would fall under exemption under the proposed amendment.

Mr. RITCHEY. Well, that is another sticky proposition that really bothers me.

Senator MATHIAS. If I can try to pull this together, I think that today's hearing on Senate bill 1739 has supplemented the record that was previously assembled by the Subcommittee on Patents, Copyrights and Trademarks.

As you know, the subcommittee did approve Senate bill 1739 for consideration by the full committee on May 21, which is 2½ months ago now. And before we did that, we had had two extensive hearings and we had made some changes in the bill.

The changes that we made were in direct response to the criticisms of consumers and of industry representatives. We heard the cry, "don't tax tapes" so we assessed the royalty only on the audio recording equipment, and blank audio tape and all video recording equipment is exempted from the bill that is before the committee today.

We heard the concern that the bill, as Mr. Ritchey has said, will only enable the rich to get richer. We have heard that before, so we have provided the Copyright Royalty Tribunal with very specific instructions to follow in the distribution of the royalty fees.

I believe that the bill that is before us goes far to ensure that all those who participate in creating America's music will be compensated when the fruit of their labor is taken without their permission.

Now, there is overwhelming evidence that advancing technologies continue to impair the ability of the law to maintain the integrity of copyright protection, and we have heard some information about the latest generation of that copying technology this morning.

While most of us would not want to inhibit technological progress, I think we cannot ignore the threats that it creates to the rights of creators, the legitimate legal rights of creators founded in the Constitution. Both are part of the bargain that is contemplated by the Constitution's copyright clause.

Now, I think that Senate bill 1739, as approved by the subcommittee, does achieve some balance between these two interests. In my opinion, certainly, it is the most important copyright bill on the Senate's agenda, and I hope that the committee will act very promptly to approve it after this hearing.

It has been good this morning to see some friends in the room who have been following this issue for many years, some of whom have been very regular participants in these hearings. I think it is significant that there are some new faces; for example, the representatives of the administration which presented its views on this matter for the first time.

Although it is not a new subject, it is the first time the administration has taken a position. I recognize that the view that was expressed does not exactly parallel my own, but the fact is that the administration does agree that home taping presents an unacceptable intrusion into the rights of copyright holders.

That position taken by the administration, I think, is an important milestone in this whole process, and I am glad to have the administration join in the effort to promote the arts and to provide American consumers with a rich and diverse selection of recorded music. I look forward to working with the administration as well as with members of the committee toward this end.

So we are very grateful to all of you for being here. We appreciate your attendance and your participation.

The committee will stand in recess, subject to the call of the Chair.

[Whereupon, at 1:41 p.m., the committee was adjourned.]

APPENDIX

ADDITIONAL SUBMISSIONS FOR THE RECORD

MEMBER OF THE BAR OF THE DISTRICT OF COLUMBIA

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April 17, 1986

Subcommittee on Patents, Copyrights
and Trademarks
Senate Committee on the Judiciary
Room SD-137, Dirksen
Washington, D.C. 20510

Re: Comments on S. 1739 & related proposals.

Dear Sirs:

I represent V.S.O.P. Records, Hindsight Records, Macola Record Co. and the Artists Rights Enforcement Corp. and have been requested by these entities to present their concerns and views regarding the Home Audio Recording Act and proposals to collect and distribute royalties collected pursuant to it. V.S.O.P. Records is a small independent record label specializing in re-releases of Jazz recordings of the 50's and 60's, as well as producing new recordings by young or under-appreciated Jazz musicians. Hindsight Records specializes in producing Big Band and related recordings from transcriptions and other sources that are not owned by the major record companies, making available numerous historically important recordings that would otherwise never see the light of day. Both companies are primarily devoted to the preservation of America's musical heritage. Macola Record Co. is a small independent record manufacturer, which also produces "Break Dance" or "Rap Music" recordings by new artists. The Artists Rights Enforcement Corp. is an organization which represents the rights of recording artists, including among its clients, Little Richard, Chubby Checker, Jan & Dean, The Coasters, The Drifters, Gene Pitney, B.J. Thomas, and many more.

As a group, there are numerous aspects of the proposed bill and subsequent proposals submitted by the RIAA/NMPA/AFofM, etc that we could support, but there are many more that will only increase the competitive imbalances that already exist in this industry, and that we oppose. In general, we all favor some solution to the home taping problem, and while we are skeptical of attempts to enact technological restrictions on importations of reproduction equipment through the Copyright laws, we do favor discussion and possible implementation of some technological solution. We are somewhat concerned about the fact that such a technological solution might be under the exclusive control of the major record companies leaving independents like ourselves selling only unprotected copies. More important is the fact that this proposal offers no solution for the present, as existing tape machines will not be affected.

Of far greater concern to us is the proposal to tax blank tape, and then redistribute the proceeds to private parties based upon a formula which only serves the limited interests of those submitting the proposal. While S. 1739 suggests a compulsory license scheme, S.1739 contemplates collection of the royalty imposed on all blank tape and all recording devices, regardless of whether the ultimate use is to copy music or for some other purpose. There is no provision for dealing with un-copyrighted music which was produced prior to 1972, and in fact, none of the proposals for distribution contemplate including artists and companies which re-release this music in their scheme. In effect, because there is no necessary connection between copyrights and the use to which blank tape might be put, this bill is a tax on blank tape. We are not opposed to such a tax. However, we are opposed to characterizing it as a copyright royalty and setting up a system of distribution of the proceeds whereby only the major record companies, their artists and publishers, and the unions receive any direct benefit.

At the heart of the problem, as we see it, is the fact that the music industry, if it can be called such, is oligopolistic, with only a small number of major recording companies controlling the type of music which the public receives and through large and highly questionable expenditures for radio play promotion, controlling what is played on radio. The proposal for distribution submitted by the RIAA/NMPA/AF of M, etc. is designed to ensure that all proceeds from collections on blank tape are distributed in such a fashion that the recordings, artists, and publishers of music which they control will receive proceeds. In effect, the proposal creates a subsidy benefitting only the most powerful and dominant elements in the market. It would act to further reduce competition in an already anti-competitive market by allowing these companies, artists and publishers to receive a significant added profit for the sale of tapes which may or may not be used to copy their materials. Naturally, the methods chosen for determining how distributions are to be made would rely on existing mothods of measuring sales and radio air-play, which methods are already skewed entirely in favor of these entities. The clients I represent are already significantly disfavored and intentionally underrepresented in all current statistics used to measure record sales and radio air play. We do not believe that the public interest can be served by further encouraging concentration of power and profits in this industry which already suffers from an excess of it. If a legitimate use of the proceeds from collections on a blank tape levy or tariff which would benefit the entire music industry can be devised, we would certainly not oppose it. We can hardly be against some added compensation for musicians and artists, who often without lasting financial reward or public recognition, have helped create some of the world's finest music. Nor are we against compensating the authors, publishers, producers and recording companies that have contributed equally as much. However, the current proposal does not really attempt to do this.

The following description of the various clients on whose behalf these comments are being made help illustrate some of the problems that these companies face in the marketplace, as well as the unfairness of the current proposals with respect to their interests.

Hindsight Records

Hindsight Records is a specialty music label devoted primarily to non-commercial recordings by bands and artists of the Big Band Era. Among their 150-200 releases are some of the finest recordings by ArtieShaw, Les Brown, Harry James, Duke Ellington, and by many lesser known artists such as Dick Jurgens, Blue Barron, Tiny Hill and many more. All recordings are fully authorized by the artists for release by Hindsight, and the publishers receive between $.60 and $.80 per record sold as mechanical royalties. While Hindsight must go to great trouble and expense in clearing the release with the artists and with the publishers, companies in Italy, for example, take these recordings off of their records and repackage them. These are then resold to American dealers at cut-rate prices, as very little or no royalties need to be paid. The reason for this occurring is that Italian Copyright Laws permit such copying and the mechanical royalty rates are extremely low in that country. Because the underlying recordings are not copyrightable, the U.S. Copyright law ban on unlawful importation does not apply when the sequence is altered or copyrighted graphics are not reproduced. While the publishers who represent the musical compositions performed on the recordings could bring infringement actions against importers and dealers of such products, they have not done so. Of far greater concern than home taping to specialty companies such as Hindsight Records is the current flood of unlawful and infringing foreign records and tapes which misappropriate the rights they have secured. To help correct this problem they would suggest that mandatory collection of mechanical royalties at Customs entry points be incorporated into the Copyright Laws. This practise is already in place in most European countries and there is no reason for the publishers to have to file infringement actions in order to collect what the law already entitles them to. In addition, they would wish that the same conditions that apply to domestic compulsory licenses apply to such import licenses to permit owners of non-copyrightable recordings to protect themselves against unlicensed imports.

While this problem has little to do with home taping, it is of far greater significance economically to companies like Hindsight than home taping could ever be. However, they are certainly affected by home taping, perhaps to an even greater extent than major record companies. Frequently, their recordings are played on non-profit radio stations during programs that feature recordings geared to the collector or appreciator of Big Band music. In addition, their recordings are frequently played on "Music of Your Life" format stations. Normal statistical air-play reporting methods neglect entirely this form of radio play. Nor do sales figures accurately reflect their share of home taping as they do a considerable amount of mail order distribution. Statistics on record sales compiled by the RIAA do not in any fashion account for these sales. In any event, as the proposal stands, unless Hindsight is credited for the air-play or sales of their copyrighted version, their injury from home taping will in no way be remedied. Nor will the outstanding artists whose recordings they release be credited. From their standpoint, the current proposal will only reward and reinforce the "hit" oriented marketing approach of the major record companies, and undermine any efforts to make important recordings available to the public. Clearly, active companies devoted to some of our greatest cultural heritage are not intended benficiaries.

V.S.O.P. Records

Like Hindsight Records, V.S.O.P. Records is a small specialty music label which employs pre-1972 recordings. V.S.O.P. Records is primarily devoted to reissuing rare jazz recordings o6 the50's and 60's. Unlike Hindsight, all of the recordings it releases were commercially produced by small independent record companies. In most cases, V.S.O.P. acquires the rights in sound recordings held by these companies or their successors, provides royalties to the artists and pays considerable mechanical royalties. Sometimes, V.S.O.P. produces new recordings, as well. As all of these recordings were commercially released, there exist means of enforcing rights held by V.S.O.P. in most countries and the problems which plague Hindsight are less significant with respect to import competition. However, there are numerous cases of piracy that occur involving these recordings, especially in Japan, the Netherlands and Spain. V.S.O.P. supports the imposition of mechanical collection procedures prior to clearance of foreign phonorecords or tapes for entry into the United States. As to home taping, V.S.O.P. Records is very concerned about the proposal as it stands. In particular, unless re-issues are given the same status as recordings that have been produced since Copyright protection was granted, reissue programs like V.S.O.P.'s will be severely disadvantaged. As in the case of Hindsight, V.S.O.P. recordings are frequently aired on NPR and other non-commercial stations, as these constitute the vast majority of radio stations that play jazz. Many stations devote special programs to the label on a periodic basis, which offers convenience to the home taper, permitting him to obtain a sample of the music without purchasing the records. While this is not all nefarious, as many home tapers later purchase the records, there is probably as much or more home taping of V.S.O.P. as there is of any major record company jazz release. While V.S.O.P. supports a tax on blank tape, it cannot support the distribution proposal since it might not include its artists or releases within the pool of distributees. V.S.O.P. is primarily distributed by mail order and there are no statistics currently kept which track those sales.

Macola Record Co.

Unlike Hindsight and V.S.O.P., Macola Record Co. produces new recordings of young artists performing "Rap" or "Break Dance" music. Its artists include the L.A. Dream Team, the Timex Social Club, Uncle Jam's Army and many other artists you may not have heard of if your only exposure to this type of music is from the radio. The reason for this is that Macola does not employ nor rely on radio play for promotion. Instead, these recordings are promoted in clubs, performances, by word of mouth, and in the record stores. Despite the lack of air-play, these recordings sell in the hundreds of thousands per title on a 12" single format. Almost all records sold are recopied for play in stereo cassette players. In fact, this format is probably the most copied format since most consumers of this music buy records but listen and play only cassettes. As the proposal stands, Macola would not benefit at all since neither its sales nor air-play of its records figure in the statistics that are currently kept. Indeed, while very few of the records produced and released by Macola end up on the charts, a majority of these records have sales figures that equal or exceed recordings that have charted. Possibly this is due to the manner in which this kind of music is surveyed in compiling the charts or the venues and clubs that are polled. Whatever the reason, present statistical methods have regularly under-reported or ignored their sales and if used to support distribution of proceeds of a tape levy of tariff, would disadvantage both Macola and its artists. Consequently, while they support a blank tape tax and distribution of the proceeds, they do not support the current RIAA/NMPA/AF of M, etc. proposal.

Artists Rights Enforcement Corp.

Unlike the last three companies, Artists Rights Enforcement Corp. is not a record company or label, but rather represents the interests of various artists such as Little Richard, Gene Pitney, The Platters, The Drifters, Chubby Checker, Lloyd Price, Bo Diddley, etc. and many more recording artists. Most of these artists recorded during the 50's and 60's for small and larger independant record companies. Few of these companies remain in business, and their successors customarily neglect to honor recording contracts, paticularly insofar as artists royalties are concerned. To further exacerbate the problem, many of their recordings have found their way into illegal recording master lease "tax shelters" and have been sold around the world to various companies which exploit them without paying any royalties. As in the case of Hindsight "knock offs", these recordings are packaged into low price compilations in countries like Italy, the Netherlands, Germany, and England, and are then marketed at cut-rate prices in the United States. In fact, not only are these artists cheated out of recording royalties, but they are cheated out of their share of songwriting royalties due on sales in the United States. Not only do these foreign recordings displace sales by U.S. licensees who pay royalties, but they devalue the artists performance in the marketplace because of the low price at which they are sold. While some of the major recording companies do employ these recordings and pay royalties for their sales, they also enter into questionable licensing arrangements with foreign and domestic companies, allowing them to manufacture tapes and records of the same performances without paying the artists. This is a case where a large block of valuable and important musical properties has been exploited to the point of ruining its intrinsic value to the detriment of no one but the artist.

At the same time this music is one of the fastest growing radio formats. Combined with current hit material, the "Classic Rock" format has become very popular. This phenomena can be confirmed by sampling radio play in most urban areas. Under the current proposals, a large segment of the music played on these stations would not be considered in computing distributions and these artists would continue to suffer the abuse they have been treated to in the past. To the extent that an even-handed method of distribution can be devised, Artists Rights Enforcement Corp. and its clients can only support a proposal which compensates the artist who recorded prior to 1972, and only recognizes sales of authorized releases.

Conclusion

As these comments indicate, home taping is a problem but probably not the most serious problem plaguing these various independent concerns. Far worse is the problem of illegal and unauthorized imports, or the problems associated with collecting artist royalties when one is no longer at the top of the charts. Recent press attention to payola and cut-out recordings merely scratches the surface of an industry oppressed by the concentration of wealth and power in the hands of too few. We cannot support further rewards and encouragement for those that probably need it the least and certainly do not deserve it. I hope that we have helped clarify some of the problems that many face today in music production and marketing. If there are any matters which you would like further information on, please contact me at (301) 340-9326, or at the addresses on the letterhead. I thank you in advance for your considered attention to these matters.

Sincerely,

Peter J. Jacobson, Esq.

The following is the name and address of each entity on whose behalf these comments were made. A contact person is provided, and if there is the need or desire for further information or testimony from any of these organizations, that person will be more than glad to assist you. In addition, I will also assist you in any way that I can.

Peter J. Jacobson

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(315) 769-2448 Contact: Thomas Gramuglia

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Macola Records Co.
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(213) 469-5821 Contact: Don MacMillan

Artists Rights Enforcement Corp.
250 West 57th Street
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(212) 586-2500 Contact: Chuck Rubin

STATEMENT
OF
JOHN C. HALL, JR., NATIONAL EXECUTIVE SECRETARY
AMERICAN FEDERATION OF TELEVISION AND RADIO ARTISTS (AFTRA)
IN SUPPORT OF
THE HOME AUDIO RECORDING ACT
S. 1739

I am John C. Hall, Jr., the National Executive Secretary of the American Federation of Television and Radio Artists (AFTRA), AFL-CIO. AFTRA is the collective bargaining representative for over 70,000 actors, singers, dancers, newspersons, announcers, disc jockeys, and other professional performers who entertain and inform the American public from coast to coast on television, cable, radio, slides, films, and sound recordings. On copyrighted sound recordings all of the voices heard whether singers, narrators, or announcers are or should be AFTRA members.

It is for this reason that we have watched with growing concern as the effects of the unauthorized taping of copyrighted sound recordings have beset the sound recording industry.

Among the more significant of those effects are --

- a decline in employment in the recording industry from 29,000 to 21,000 between the years 1978 and 1982;
- annual losses in sales of copyrighted sound recordings of $1.5 billion because of the unauthorized taping of sound recordings; and
- a precipitous reduction in the number of new sound recordings released so that today the number is less than one-half of what it was six years ago.

This is all a part of the record and I shall not dwell on it further. But given the data it is manifest that the unauthorized taping of copyrighted sound recordings has had a disastrous effect on the recording industry and most of those who earn their livelihood in it.

As I read the Home Audio Recording Act -- S. 1739 -- it would exempt from copyright infringement liability individuals who make copies of copyrighted sound recordings for their personal use.

Importers and manufacturers of audio recording equipment and blank audio tapes capable of recording music in the home would be licensed to distribute their equipment and tapes in the United States in return for the payment of royalty fees on those items.

The legislation prescribes that the royalty fee on standard audio recording equipment will be 5% of its wholesale price. Dual audio recording equipment, those devices capable of dubbing directly from tape to tape, would bear a royalty rate of 25% of the wholesale price. Audio recording equipment capable of dubbing two or more tapes (which are clearly designed for copyright violations) would be excluded from licensing. Thus, it would be a violation of law to sell or distribute them in the United States. The royalty fee for blank audio tape is fixed in the bill at one cent per minute of playing time.

Under the legislation, the Copyright Royalty Tribunal (CRT) could exempt audio recording equipment and blank tape (1) which it found to be unsuitable for home taping of recorded music, or (2) which was used in a trade or business or for professional purposes and not for the home taping of recorded music.

Royalty fees, under the legislation, would be paid to the Register of Copyrights who after deducting the reasonable costs of administering the legislation would deposit them in interest bearing securities in the U.S. Treasury.

Copyright owners of musical works or sound recordings which were broadcast in the United States or sold as records or tapes could file claims against the pool of royalty fees with the CRT which would distribute the fees among the claimants after deducting its reasonable costs of administration.

The legislation would take effect on January 1, 1987.

Thus, the legislation carefully balances the interests of those affected by the home taping of copyrighted works — those who engage in the practise, the manufacturers and importers who provide the equipment and tape which make home taping possible, and the copyright owners whose property is appropriated by home taping.

In addition, S. 1937 resolves the problems which beset its antecedent, the Home Recording Act of 1983. It provides for the exclusion of audio recording tape and equipment neither intended or suitable for the recording of music and of equipment and tape used in a trade or business or for professional purposes and not for the home taping of recorded music.

The Home Audio Recording Act, S. 1739, is good legislation. I urge its enactment.

STATEMENT OF LEE RICHARDSON

PROFESSOR AND G. MAXWELL ARMOR EMINENT SCHOLAR

S.1739 establishes some major new mechanisms which will affect not only copyright owners, but also manufacturers of recording devices and supplies as well as the consuming public. Retailers and allied businesses are also to impacted.

S.1739 does not appear to benefit consumers directly or indirectly. It will be costly to the consuming public, I fear, and the proposal does not establish a mechanism which can be reasonably expected to benefit music creators.

The subcommittee and its staff have discussed many concepts and have been open to the varied views of many persons. I appreciate the personal opportunities that I too have been afforded to provide a consumer view.

I believe a number of problems and concepts are emerging on which many persons agree at this early stage in the legislation's history. One problem is that of the particular amounts of royalties which might be applied under any reasonable standard to particular tapes, cassettes or recording devices. The amount of any of the bill's royalties should be carefully reconsidered. The dollar impact on prices paid by the public is, very difficult to estimate and can only said to be substantial.

There should be a clear definition of "private use" that includes gifts and similar non-commercial uses and that all of this type of private use should be exempt from any liability for infringment of copyright.

Participation of persons or organizations with relatively small claims on the royalty fees will be exceedingly difficult. Some streamlined provisions for such claimants, many of whom will be emerging creative artists, is essential.

Possible exemptions for equipment and media found "unsuitable for making audio recordings for individuals for private use" are left entirely to the discretion of the Tribunal. It is an exceedingly broad delegation to an agency without resources and track record to justify such a delegation. In fact the Tribunal could deny any exemptions.

"Noninfringing uses" is a similarly unrestrained or unrestricted delegation. It is only fair to have such exemptions made available to consumers, but the legislation gives no assurances that any mechanism can be devised that is both fair and inexpensive to administer nationwide for every tape and equipment purchase.

Future adjustment of royalty fees in the proposal could assume that all private audio recordings result in denial of compensation for copyright owners. This could lead to an absurdly high royalty fee adjustment upwards. More serious is the fact that the very general principles in S.1739 effectively make final determination of adjustments wholly matters of judgment by the Tribunal. There are simply no limits or objective standards imposed on the agency.

The definition of audio recording would exempt any technology that permits visual images as well. Videotapes can already be used for high quality aural recording.

Audio recording devices as defined could embody almost all such devices now on the market. Only special new products developed and marketed at considerable cost to the producers (and passed through to their customers at appropriate markups) would be exempt. This government created market would be an artificial and costly one just to avoid the mandated royalty fees. This artificial market will not be easily developed due to the considerable quantities of equipment which will be sold prior to the implementation of the royalty fee system.

There is little reason to believe that an interested and not yet marketed technology can be developed for this artificial market. Any "unsuitable" device which can record at all can be made suitable again at some cost. If that cost is low enough, "unsuitable" devices will have to be declared suitable. The existing "unsuitable" devices will have defeated the royalty system.

"Audio recording medium" is defined in such a way that it already admits to a serious future problem. A prerecorded tape with easily erased content can avoid the royalty unless it is found to be trying to "avoid the obligations" of paying the royalty fee. This could be a monstrous administrative problem that defeats the royalty fee system. It could also be difficult for small businesses and organizations to buy exempt tapes and produce prerecorded products. In any event the tribunal will have no legislative guidance on how to solve this dilemma.

The "dual audio recording device" definition is quite specific. The high royalty fee on such devices may be easily be avoided by a cable between two "single" devices. The effect of the royalty will then have been to destroy the market for dual devices.

The "multiple audio recording device" definition attempts to anticipate future technological developments. It too may lead to market adjustments which are costly or have undesired or unanticipated consequences.

While the legislation is aimed at devices and media which interface with transmission systems, the royalty fees will encourage new technologies or commercial systems that bypass transmission systems.

There is no provision whatsoever for participation by consumers; i.e., the parties whose private use is at issue in this legislation. The consumer interest will not be effectively represented without funding or procedural improvements to remedy the wholly unacceptable processes employed by the Tribunal under its existing authority and appropriations. This legislation is unique in its many impacts on consumers and thus it will require reliable and accurate inputs concerning private use and the decisions consumers will make if the Tribunal elects various proposals which will come before it. In view of the broad delegations of authority to the Tribunal, consumer participation must be enhanced to insure that the Tribunal will make good public policy decisions.

The legislation on the whole is devoted to problems of collecting and distributing fees to copyright holders. It does not address how copyright holders will in turn distribute those funds to enhance creative activity. It is altogether possible that these funds will be used to build sales of the products of established artists, be paid to owners, or be used for investments entirely unrelated to the music industry. The implicit trickle down theory that somehow artists will be encouraged to be more creative cannot be assumed.

The copyright system may not achieve its purpose of encouraging musical artists as well as other approaches might do so. Direct grants and support may be more practical. The National Endowment for the Arts might be far more efficient in targeting artists than the copyright legislation's broad and indirect impact can ever be. After all, it is not the intention of this legislation to improve the relative bargaining position of commercially minor or emerging artists vs. a vs. the large companies that will often own copyrights on their music.

Modern music production involves many creative and technical specialists. A single artist as such is something of a romantic myth. There is little known about how the windfall of royalty fees might be distributed among so many different contributors to "artistry" in music as well as to owners, other suppliers of capital, agents, marketings and advertising, ad infinitum.

The problem cannot be measured accurately. The lost sales and revenues of the industry are highly speculative numbers about which expert research firms do not agree. Even if it were an amount agreed to, lost sales do not translate to lost incentives for artists who therefore choose not to create. Artists, unlike some business managers (or even business professors, I suspect), are not simply greedy economic men who will product more creative art in proportion to royalty fee incentives.

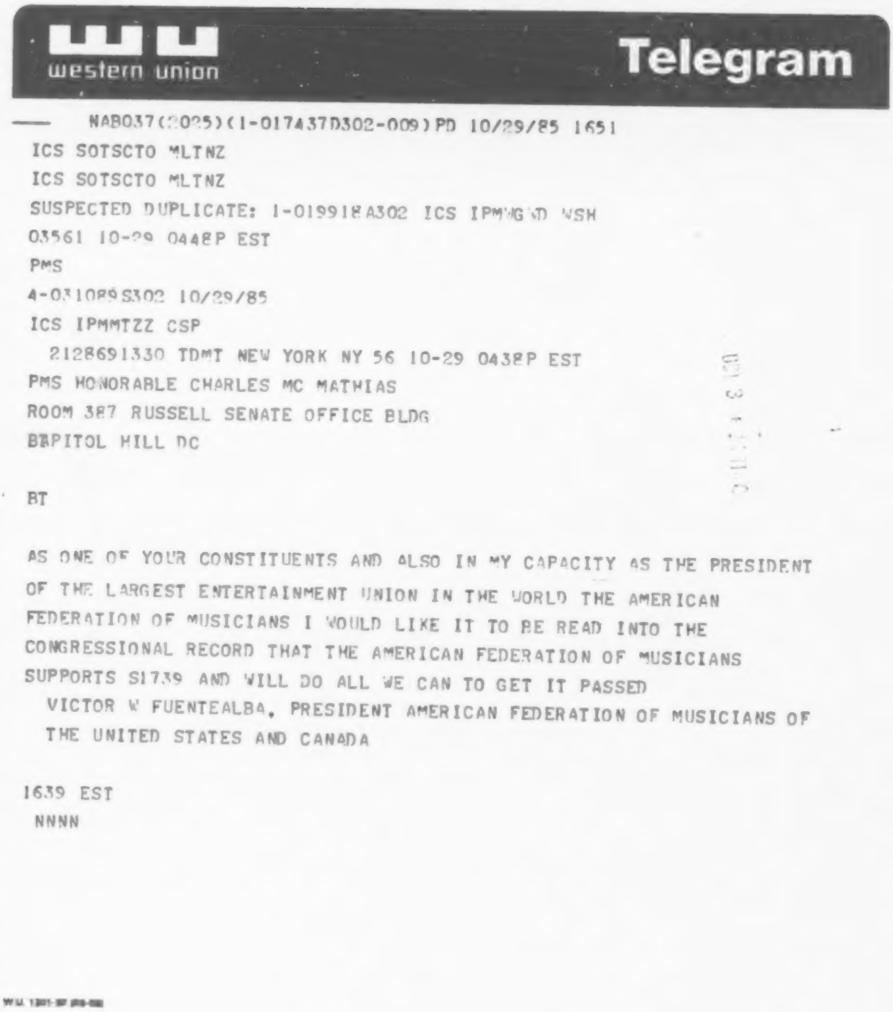
Consumers find the idea of a royalty fee imposed on private music taping difficult to accept for any purposes because no one has raised the problems alleged to exist by this legislation until now. Why must a thriving industry have government step in to provide royalty fees to record companies in 1985 when private recording has been widespread since about 1950?

The fact that private use has been permitted, de facto, since 1950 makes the claims that it is not clearly legal seem preposterous to consumers.

The legislation does not follow through in any discernable way on the innocuous claim of the "Dear Senator" letter of September 26. It states that the forthcoming bill "would impose a small royalty fee on some tape records and on a limited category of high quality blank tapes." In reality it would impose a significant royalty fee on almost all currently available tape recorders and a punitive fee on dual cassette recorders. It would add $.90 to 90 minute blank tape production costs and a much higher cost downstream to consumers at retail sales points. It may include all tapes for it requires virtually no exemptions or exceptions to the royalty based on use. It does not provide any definition of high quality, but instead would only exempt tapes which cannot record music suitably for some unknown technical reasons. High quality tape thus may include all tapes rather the alleged limited category.

S.1739 is disappointing. It does not seem necessary or desirable. It will be costly and burdensome to consumers. It will cause consumers who do not tape music to pay fees they to do not fairly owe to the owners of music copyrights. It will raise costs of tapes and recording devices by many millions of dollars literally every week without a reasonable expectation than even a small portion of it will stimulte musical artistry anywhere.

CORRESPONDENCE



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BT

AS ONE OF YOUR CONSTITUENTS AND ALSO IN MY CAPACITY AS THE PRESIDENT OF THE LARGEST ENTERTAINMENT UNION IN THE WORLD THE AMERICAN FEDERATION OF MUSICIANS I WOULD LIKE IT TO BE READ INTO THE CONGRESSIONAL RECORD THAT THE AMERICAN FEDERATION OF MUSICIANS SUPPORTS S1739 AND WILL DO ALL WE CAN TO GET IT PASSED

VICTOR W FUENTEALBA, PRESIDENT AMERICAN FEDERATION OF MUSICIANS OF THE UNITED STATES AND CANADA

1639 EST
NNNN

WU 1201 [illegible]

UNITED STATES DEPARTMENT OF COMMERCE
Patent and Trademark Office
Address: COMMISSIONER OF PATENTS AND TRADEMARKS
Washington, D.C. 20231

Honorable Charles McC. Mathias, Jr.
Chairman
Subcommittee on Patents, Copyrights
and Trademarks
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for your letter inviting me to testify on S. 1739, a bill to amend the copyright law as it affects the home audio recording of copyrighted material. This is an important topic that affects the interests of many segments of society including music composers, sound recording producers, and the general consuming public. It is clear that you and this bill's other sponsors have recognized these interests and tried to deal with them.

The Administration, however, is not prepared to testify on S. 1739. This does not imply a lack of concern, but rather we cannot conclude whether the formula adopted in this bill is just and fair because the information available to us is not only conflicting but incomplete. Consequently, I would prefer to defer my testimony on this topic until this issue can be studied in depth and an Administration position established. I expect that the information provided to your Subcommittee in the hearing on this bill will be of assistance to the Administration in formulating its position.

Sincerely,

Donald Quigg

Donald J. Quigg
Assistant Secretary and Commissioner
of Patents and Trademarks

INTERNATIONAL ALLIANCE OF THEATRICAL STAGE EMPLOYES AND MOVING PICTURE MACHINE OPERATORS OF THE UNITED STATES AND CANADA,
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OFFICE OF THE PRESIDENT

November 12, 1985

Senator Charles McC Mathias
Chairman
Subcommittee of Patents,
Copyrights and Trademarks
Senate Committee on the Judiciary
137 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Mathias:

The International Alliance of Theatrical Stage Employes and Moving Picture Machine Operators of the United States and Canada, AFL-CIO, hereby goes on record in support of, and urges passage of S. 1739.

We believe the Home Audio Recording Act is a fair and equitable resolution of the home audio taping issue and will permit the consumer to benefit from a continuing diversity of sound recordings, as well as improved audio recording devices and tapes.

At the same time, the performers, writers, technicians and crafts people who produce sound recordings will be fairly compensated for the use of their work.

Kind regards.

Sincerely,

Walter F. Diehl

Walter F. Diehl
INTERNATIONAL PRESIDENT

WFD:ls

STANFORD LAW SCHOOL, STANFORD, CALIFORNIA 94305

PAUL GOLDSTEIN
STELLA W. AND IRA S. LILLICK PROFESSOR
OF LAW

17 January 1986

Senator Charles McC. Mathias, Jr.
Chairman, Subcommittee on Patents,
Copyrights and Trademarks
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Senator Mathias:

Thank you for your letter of 4 December inviting me to comment on S.1739. The Bill addresses a very important issue, and I am pleased to have the opportunity to comment on it.

In my judgment, S.1739 represents a practical, principled and, in general, a desirable, resolution of the home audiotaping question. Thus, I will confine my comments in this letter to three points: (1) Why the approach taken in S.1739 generally conforms to traditional copyright principles; (2) How small changes in the text of the Bill, or the inclusion of appropriate language in the accompanying Senate Report, might make S.1739 conform even more closely to traditional copyright principles; and, in response to a specific question that you raise in your letter, (3) Why technological means for preventing home audiotaping are inferior to legal means such as S.1739.

(1) *The approach taken in S.1739 generally conforms to copyright principles.* In his excellent testimony before your Subcommittee on 30 October, Register of Copyrights Ralph Oman accurately cut through the rhetoric surrounding discussion of home taping to identify the "real issue": "Should the copyright law provide compensation for copyright proprietors for unauthorized reproduction of copyrighted works?" The historical premises and development of copyright law in this country dictate an affirmative answer.

Congress has historically extended the reach of copyright to encompass new uses of copyrighted works, clarifying existing rights and defining new ones as new areas of economic activity deriving value from copyrighted works have emerged. In the beginning, the principal use of copyrighted works was reproduction in copies, and the first American copyright act accordingly conferred "the sole right and liberty of printing, reprinting, publishing, and vending" copyrighted works. As new uses of copyrighted works assumed economic significance, Congress responded by extending copyright to assure that at least part of the economic value of these new uses was returned to the copyright owner. Thus, over the course of the first century of the U.S. Copyright Law, as performances, dramatizations, translations, abridgements, and adaptations generally, acquired economic significance, Congress extended the scope of copyright to cover these activities in 1856, 1870 and 1909 respectively.

One important trend over the past century has been the evolution of economically significant uses of copyrighted works away from centralized, readily discernible uses -- such as reproduction by a competing publisher -- toward decentralized uses -- such as broadcast performances, school and library photocopying, and home taping. Transactionally, the trend has been away from uses respecting which the copyright owner could conveniently negotiate with a small number of centralized users, and toward uses which it is impractical for the copyright owner to locate, and respecting which it is impractical for the owner to negotiate with those who are deriving economic value from the copyrighted work.

Recognizing this phenomenon, Congress has historically observed an important limitation on the extension of rights to cover new uses: where transaction costs -- the costs of identifying and negotiating with users -- are likely to hobble the fluent market transfer of exclusive rights, Congress has been careful not to extend exclusive rights, lest the existence of the right, and the inability of the potential user to negotiate a license, prevent a valuable use from being made. Thus, over the past century, Congress has perceived the need to strike a balance between the principle that copyright proprietors should be compensated for all uses that derive value from their works and the reality that to extend exclusive rights against some of these uses may, because of the problem of transaction costs, prevent that use from being made.

Congress has, however, consistently viewed the principle of compensation as paramount, and has recognized that if transaction costs could be appropriately reduced, the right should be extended to cover the new use. Where market mechanisms -- clearing houses like ASCAP, BMI and the Copyright Clearance Center -- evolved to reduce transaction costs respecting the relevant right, Congress wisely retained the principle of exclusive rights. Where the emergence of cost-reducing market mechanisms was not perceived as likely -- as evidently was the case with cable retransmissions and jukebox performances -- the less desirable alternative of nonexclusive compulsory licenses was adopted.

Accommodation of the principle of compensation with the practicality of transaction costs has thus historically produced compromise. S.1739 represents just such a compromise. Because audiotaping in the form contemplated by the Bill characteristically involves private activity, the Bill's allocation of liability to manufacturers of equipment and media, rather than to home users, represents a prudent concession to the transaction costs that surround private use. Although the Bill would expressly exempt private audiotaping, it correctly recognizes that the privacy of the activity affects only the remedy employed and not the right that is at stake. To state the point bluntly, the individual who tapes a composition off the air or from a phonorecord deprives the copyright owner of value just as surely as he would if he used his home computer to divert funds from the copyright owner's bank account into his own. By placing liability on suppliers, who will presumably pass some of its costs on to consumers, S.1739 strikes a balance that honors both the principle of compensation and the interests of reducing transaction costs.

(2) Small changes in the text of S.1739, or the inclusion of appropriate language in the accompanying Senate Report, might make the Bill conform even more closely to traditional copyright principles. Marketplace or legal innovations aimed at reducing transaction costs usually entail compromise. In the case of S.1739 the compromise is with three principles: (a) that privately negotiated bargains between owners and users are preferable to compulsory licenses; (b) that consumers should pay only for what they consume; and (c) that producers should be paid only for what they produce.

(a) In light of existing market patterns, the compulsory license effected by S.1739 represents an appropriate, possibly transitional, vehicle, assuring that some compensation will be paid to producers while not allowing transaction costs to disable uses by consumers. I would underscore the word "transitional." If, at some point, market forces become so configured -- through the vehicle of clearinghouses, possibly, or though the evolution of new technological capabilities -- that transaction costs can be minimized without resort to a compulsory license, I believe that it would be appropriate for Congress to reconsider the compulsory license and to consider a return to the standard statutory pattern of exclusive rights.

(b) To the extent that the compulsory license fee paid by manufacturers is passed on to consumers, consumers who are using machines and tapes for purposes other than copying copyrighted works will understandably complain that they are paying for goods or services that they have not consumed. One answer to this complaint is that this is an attribute of compromise with which we have learned to live in a civil society. The homeowner who pays a real property tax that is devoted in part to the maintenance of swimming pools and schools in his or her community, must pay that tax even though he or she neither swims nor has children attending school. This is a necessary cost of an imperfect solution. In any event, in light of the facts adduced in the testimony before your Subcommittee, and under the structure of S.1739, the possible discrepancies between payment made and value received are likely to be far smaller than ones we have come to tolerate in other areas.

Second, §§119(c)(1)(E)(i) and (ii) seem well calculated to reduce these discrepancies. Your Subcommittee might consider, in addition, a direction to the Copyright Royalty Tribunal, pursuant to §119(c)(1)(E)(ii), to promulgate a regulation under which anyone who purchased a tape or machine that he or she did not use for infringing purposes, could execute and submit a form, under the terms prescribed by the CRT, affirming that the tape or machine was not used for these purposes, and would consequently receive a rebate from the CRT. To be sure, such an approach would entail transaction costs for the submitter and the Tribunal; but these costs will doubtless be lower than those entailed by an exclusive right against private taping.

(c) Some concern may also be expressed that producers will not be compensated according to the popularity -- i.e. the frequency of recording -- of the works that they produce, with some producers overcompensated and others undercompensated. As §119(b)(5)(A) quite properly contemplates, producers can be expected voluntarily to develop systems for proportioning compensation to use, and an antitrust exemption for this purpose seems a desirable feature. Although it may be sufficient to rely on private initiative among producers for these purposes, some specific direction to the Copyright Royalty Tribunal to attempt to proportion returns to use may be desirable as a goad to properly directed bargaining among producers.

(3) Technological means for preventing home audiotaping are inferior to legal means such as S.1739. Failure to enact S.1739, or some similar bill, may very well encourage copyright proprietors to develop technical mechanisms designed to prevent replication of their recorded works through home taping. I think that, for at least three reasons, this would be an undesirable development. And, for the same reasons, I think it would be singularly undesirable for Congress, as an alternative to S.1739, to mandate the implementation and incorporation of devices in machines, preventing the duplication of recorded works.

First, any investment in the production of encryption or other anti-copying technologies will represent a wasteful expenditure. Time, money and talent that might be better devoted to technological invention yielding social benefits would instead be channeled toward investment aimed only at preventing a harm that could be avoided at lower cost through the adoption of a legal rule like S.1739. Laws against trespass to land are preferable to, because less costly than, expensive fences built to keep out poachers. The same principle applies to copyright.

Second, and also from an economic viewpoint, this investment in technical barriers is undesirable because it will simply lead to more, and more wasteful, investment aimed at tearing down the barriers. As we know so well from the computer software area, efforts at encryption only lead to counter-efforts at disencryption. Once again, society would be better off if creative minds applied themselves to other, more socially productive innovations.

Third, from a political perspective, I believe that resort to technological mechanisms as a substitute for legal rules runs a significant risk of impairing fidelity to legal rules overall. If fidelity to copyright law is to be maintained in the areas of other uses, we should avoid programs that effectively represent concessions to illegality in any area, as would a program that conceded the disutility of copyright law as a vehicle for assuring that copyright owners be compensated for the audiotaping of their works. To legislatively mandate such anti-copying devices seems likely to impair fidelity to copyright law even more substantially.

I hope that these observations will be of use to you and your Subcommittee in your deliberation on S.1739. If this letter raises any questions, or if there are any points that you would like elaborated, please do not hesitate to call on me.

Cordially yours,

Paul Goldstein

PG/mmek

National Consumers League
Founded 1899

815 15th Street NW • Suite 516 • Washington, DC 20005 • (202) 639-8140
Linda F. Golodner, Executive Director

April 21, 1986

The Honorable Charles Mathias
Chairman, Subcommittee on Patents,
Copyrights and Trademarks
Senate Judiciary Committee
Washington, DC 20510

Dear Chairman Mathias:

We are writing to express our support for S. 1739, the Home Audio Recording Act. We support the Act because it promotes two fundamental goals of the National Consumers League - economic justice in the marketplace and a fair compensation for workers.

The National Consumers League introduced the concept of minimum wage to this country, and throughout its 87-year history, it has worked for economic and social justice. It is our belief that we consume the work and labor that have gone into the goods we use. Our support for legislation to provide for compensation to artists and producers of music is consistent with, and an outgrowth of, the League's historic concerns.

We support the Home Audio Recording Act because it permits consumers to copy pre-recorded music, while at the same time it ensures that compensation will flow to the copyright owners whose property is being taken, and to the artists and other workers whose labors have made those recordings possible.

Some people regard unauthorized home taping as beneficial to consumers - after all, they can obtain pre-recorded music without paying for it. The same could be said, however, for commercial record piracy, which also offers lower prices to consumers. As with piracy, the "benefits" to consumers of uncompensated home taping are short-term and illusory.

Consumers lose out when the variety of pre-recorded music available to them is reduced. All the available data suggests that the growth of home taping has contributed to a diminution in the amount of new music released. Compensating

Officers: Robert R. Nathan, Honorary Chairman • Esther Peterson, Honorary President • Jack Blum, President • Esther Shapiro, Vice President • Bert Seidman, Vice President • Ruth E. Kobell, Secretary • Virginia Klutts, Treasurer

artists and producers for some of the revenue they lose from home taping would help counter that trend by encouraging investment in music which today may be considered too risky or too limited in appeal. Moreover, the Musical Arts Endowment and the system of Creative Incentive Grants suggested by the music community at the March 25, 1986, hearing of your Subcommittee will further support and encourage the diversity which is threatened by home taping.

Consumers lose out when talented young men and women are discouraged from pursuing careers as musicians, vocalists or composers. Yet this is precisely what will happen if the fruits of their labor continue to be freely appropriated in disregard of their right to be compensated for their work and for the use of the property which they have created. By ensuring a measure of support and such compensation, the Home Audio Recording Act will encourage the next generation of American artists to continue in their creative endeavors.

Consumers lose when those who choose not to pay for a product are allowed to get a product free while others are left to bear all the costs. Yet this is what home taping does. In fairness to those who *buy* their pre-recorded music, Congress should put an end to the inequitable "free ride" that home tapers are taking at the expense of music purchasers and the American music community.

In sum, consumers will support legislation that ensures a measure of compensation to artists and producers when that music is copied rather than purchased. They will do so because they understand that getting goods for the cheapest price is not a good deal if one ends up sacrificing things worth paying for. Providing this compensation may raise the prices of blank tape and recording equipment slightly, but it will help guarantee the continued quality and diversity of the American music that people want to tape.

American consumers have a finely developed sense of fairness. Asking those who copy pre-recorded music to pay for the privilege of doing so is fair, both to other consumers and to artists and producers of the music being taped.

The National Consumers League therefore urges you to take quick and favorable action on the Home Audio Recording Act. We would also appreciate it if you would include this letter in the hearing record on this legislation. Thank you very much.

Sincerely,

Jane M. King

JANE M. KING
Deputy Director